Petition

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81-1494

No.

In the Supreme Court of the United States

OCTOBER TERM, 1981

JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET AL.,
PETITIONERS

v.

ONILEA NEAL

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

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QUESTION PRESENTED

Whether a suit alleging a negligent failure by a Farmers Home Administration employee adequately to inspect the construction of a house that subsequently is discovered to have defects is barred by the "misrepresentation" exception to suits allowed against the United States under the Federal Tort Claims Act, 28 U.S.C. 2680(h).

PARTIES TO THE PROCEEDING *

Other parties, in addition to those named in the caption, are Charles W. Shuman, Administrator of the Farmers Home Administration; Johnny Vernon Crow, Tennessee State Director of the Farmers Home Administration; S. Lane Parkison, Roane County Supervisor of the Farmers Home Administration; and Mary Wells, Assistant Roane County Supervisor of the Farmers Home Administration.

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* Although respondent's complaint was filed against the Secretary of Agriculture and other Department of Agriculture officials, the United States is the only proper defendant under the Federal Tort Claims Act. 28 U.S.C. 2674, 2679(a).

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

The Solicitor General, on behalf of the United States and the United States Department of Agriculture, the Secretary of Agriculture, the Farmers Home Administration (FmHA), and various FmHA officials, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. C, *infra*, 4a-18a) is reported at 646 F.2d 1178. The opinion of the district court (App. D, *infra*, 19a-27a) is reported at 489 F. Supp. 512.

JURISDICTION

The judgment of the court of appeals was entered on May 1, 1981 (App. B, *infra*, 2a-3a), and a petition for rehearing was denied on September 28, 1981 (App. A, *infra*, 1a). On December 21, 1981, Justice O'Connor extended the time in which to file a petition for a writ of certiorari until February 10, 1982. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTES INVOLVED

1. Section 501(a) of the Housing Act of 1949, 42 U.S.C. (Supp. III) 1471(a), provides in pertinent part:

> The Secretary of Agriculture * * * is authorized, subject to the terms and conditions of this subchapter, to extend financial assistance, through the Farmers Home Administration, (1) to owners of farms in the United States * * * to enable them to construct, improve, alter, repair, or replace dwellings and other farm buildings on their farms, and to purchase buildings and land constituting a minimum adequate site, in order to provide them * * * with decent, safe, and sanitary living conditions and adequate farm buildings as specified in this subchapter, and (2) to owners of other real estate in rural areas for the construction, improvement, alteration, or repair of dwellings, related facilities, and farm buildings and to rural residents for such purposes and for the purchase of buildings and the purchase of land constituting a minimum adequate site, in order to enable them to provide dwellings and related facilities for their own use and buildings adequate for their farming operations * * *.

2. Section 502(a) of the Housing Act of 1949, 42 U.S.C. 1472(a), provides in pertinent part:

> If the Secretary determines that an applicant is eligible for assistance as provided in section 1471 * * * a loan may be made by the Secretary to said applicant for a period of not to exceed thirty-three years * * *.

3. Section 506(a) of the Housing Act of 1949, 42 U.S.C. 1476(a), provides in pertinent part:

> Buildings and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary. In addition to the financial assistance authorized * * * the Secretary is authorized to furnish * * * technical services such as building plans, specifications, construction supervision and inspection * * *.

4. Section 509(c) of the Housing Act of 1949, 42 U.S.C. (Supp. II) 1479(c), provides in pertinent part:

> The Secretary is authorized, after October 1, 1977, with respect to any unit or dwelling newly constructed * * * and purchased with financial assistance authorized by this subchapter which he finds to have structural defects to make expenditures for (1) correcting such defects, (2) paying the claims of the owner of the property arising from such defects, or (3) acquiring title to the property, if such assistance is requested by the owner of the property within eighteen months after financial assistance under this subchapter is rendered to the owner of the property * * *. Decisions by the Secretary regarding such expenditures or payments under this subsection, and the terms and conditions under which the

same are approved or disapproved, shall not be subject to judicial review.

5. The Federal Tort Claims Act, 28 U.S.C. 2680, provides in pertinent part:

> The provisions of this chapter and section 1346(b) of this title [conferring jurisdiction on the district courts] shall not apply to—
>
> * * * * *
>
> (h) Any claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or interference with contract rights * * *.

STATEMENT

1. The Farmers Home Administration (FmHA) is the agency authorized by the Secretary of Agriculture to extend financial assistance to eligible rural residents to help them acquire "decent, safe, and sanitary living conditions." 42 U.S.C. (Supp. III) 1471(a). FmHA may provide this assistance either by direct loans from the Secretary of Agriculture (42 U.S.C. (& Supp. III) 1472) or by insured or guaranteed loans (42 U.S.C. (& Supp. III) 1487).

Regardless of the form of the assistance, FmHA's regulations declare generally that "[s]upervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect the interests of the Government * * *." 7 C.F.R. 1822.7(a). Specifically, the regulations in effect at all times relevant to this case provided that (7 C.F.R. 1804.4(g)(3) (1980)):

> The County Supervisor will inspect development work as frequently as necessary to assure that construction and land development conforms with

> the plans and specifications. He will make a final inspection at the earliest possible date after completion of the planned development.[1]

2. In 1977, respondent obtained a Rural Housing Loan from FmHA pursuant to Section 502(a) of the Housing Act of 1949, 42 U.S.C. 1472(a) (App. C, *infra*, 5a). Thereafter, respondent entered into an agreement with a local contractor to construct a prefabricated house (*ibid.*). During the course of construction, a local FmHA official inspected the house on three occasions and signed inspection reports, none of which contained any adverse comments on the condition of the house or its compliance with FmHA plans and specifications (*id.* at 6a). Respondent, as

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[1] The Department of Agriculture amended the FmHA regulations effective June 12, 1980. 45 Fed. Reg. 39789 (1980). Section 1804.4(g)(3) was deleted and its substance was reenacted as 7 C.F.R. 1924.9(a), with the following addition:

> FmHA's inspections are not to assure the borrower that the house is built in accordance with the plans and specifications. The inspections create or imply no duty or obligation to the particular borrower but are, rather, for the dual purposes of determining that FmHA has adequate security for its loan and enabling FmHA to determine that FmHA is working toward achieving the statutory goal of providing adequate housing.

The Department of Agriculture explained the change as follows:

> [E]xisting statutes provide for these construction inspections to be conducted by FmHA personnel solely to determine adequacy of the FmHA security. Language other than that contained in the final rule may create legal problems by not properly informing the public as to the purpose of these inspections.

45 Fed. Reg. 39792 (1980). Thus, the new regulations were intended to clarify preexisting law on this issue.

well as the FmHA inspector, signed the final inspection report (C.A. App. 13-14).[2]

Two months later, respondent notified FmHA and the building contractor that the heat pump in her house was malfunctioning. An FmHA inspection disclosed 13 defects, including the heat pump, that the contractor failed to cure despite FmHA's notification and demand that it do so (App. C, *infra*, 6a). FmHA refused respondent's administrative request to pay for correcting the defects (*ibid.*).

3. Respondent then filed the instant suit in the Circuit Court of Roane County, Tennessee, against the Secretary of Agriculture, other Department of Agriculture officials who administer the FmHA program and the private builder who constructed the house. The federal officials removed the case to the United States District Court for the Eastern District of Tennessee pursuant to 28 U.S.C. 1441. After removal, respondent amended her complaint to allege causes of action based on the Tucker Act, 28 U.S.C. 1346(a)(2), and the Federal Tort Claims Act, 28 U.S.C. 2671 *et seq.* (C.A. App. 8-27).[3]

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[2] "C.A. App." refers to the Appendix filed in the court of appeals.

[3] Respondent also sought mandamus to compel the Secretary of Agriculture to compensate her, under 42 U.S.C. (Supp. II) 1479(c), for the construction defects FmHA had identified in her house (App. D, *infra*, 24a-26a). The district court dismissed the mandamus count (*id.* at 26a), and respondent did not challenge that ruling in the court of appeals.

Respondent's original state court complaint did not specify the basis for her claim as one arising solely under federal law, and (except for one brief reference to the Federal Tort Claims Act) the claim appears to have been based on state common law. She merely sued the government employees in their official and individual capacities for the costs of repairing the defects

The district court dismissed the complaint against the federal defendants for failure to state a claim and for lack of subject matter jurisdiction (App. D, *infra*, 19a-27a) and remanded the suit against the builder to state court. It reasoned that "[t]o hold the FmHA liable for the shoddy work of the contractor would be tantamount to making a mortgagee the warrantor of the quality of its security" (*id.* at 23a). The court concluded that the FmHA statutes and regulations did not create such a duty running to respondent, and that, to the contrary, the primary purpose of the inspection process was to enable the government to protect its security interest in houses financed under Section 502 (*id.* at 22a-23a).

The court of appeals reversed (App. C, *infra*, 4a-18a). The court of appeals upheld the district court's determination that the statute and regulations governing the FmHA's inspection did not give rise to a contractual duty to protect respondent from defects in the construction of her home (*id.* at 9a-11a).

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that the government negligently failed to discover. At the time the case was in state court, therefore, no one understood the suit to be based solely on the Federal Tort Claims Act and thus within the exclusive jurisdiction of the federal courts, 28 U.S.C. 1346(b). Thus, we assume that there was some residual basis for the state court's jurisdiction at the time of removal. See *McGowan* v. *Williams*, 623 F.2d 1239 (7th Cir. 1980).

In the district court, after the complaint was amended, it became clear from respondent's brief in opposition to the government's motion to dismiss (C.A. App. 50) that the basis for respondent's suit was the Federal Tort Claims Act, and the district court treated it as such. We thus believe that the district court either had jurisdiction as a result of the removal or that the amended complaint, which was filed within the statute of limitations, effectively initiated the suit in federal court properly under Section 1346(b).

It rejected, however, the district court's determination that there was no tort liability (*id.* at 11a-18a). Instead, the court of appeals found that the FmHA had breached the duty created under the common law Good Samaritan doctrine.[4] The court reasoned that the government, having voluntarily undertaken to inspect the house, was liable for all injuries caused by its negligent failure to discover any defects in the construction of the house (*id.* at 11a-13a).

In holding that respondent's complaint stated a claim under the Federal Tort Claims Act, the court of appeals distinguished *United States* v. *Neustadt*, 366 U.S. 696 (1961), as "a situation dealing with a cause of action based on misrepresentation [rather than] a cause of action based on negligent performance of an operational task" (App. C, *infra*, 16a). The court of appeals did acknowledge that its decision conflicts with *Reynolds* v. *United States*, 643 F.2d 707 (10th Cir. 1981), cert. denied, No. 80-2064 (Oct. 5, 1981), but it nonetheless was "satisfied" that respond-

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[4] The court of appeals relied on the *Restatement (Second) of Torts* § 323, at 135 (1965), which provides:

> One who undertakes, gratuitously or for consideration, to render services to another which he should recognize as necessary for the protection of the other's person or things, is subject to liability to the other for physical harm resulting from his failure to exercise reasonable care to perform his undertaking, if
>
> (a) his failure to exercise such care increases the risk of such harm, or
>
> (b) the harm is suffered because of the other's reliance upon the undertaking.

The court of appeals did not, however, establish that Tennessee law recognizes these principles, a necessary prerequisite to a finding of liability under the FTCA in any event. See *Feres* v. *United States*, 340 U.S. 135, 141-142 (1950).

ent "is entitled to go forward with her case" (App. C, *infra*, 18a n.7).

REASONS FOR GRANTING THE PETITION

The decision of the court of appeals cannot be reconciled with this Court's decision in *United States* v. *Neustadt*, 366 U.S. 696 (1961). In *Neustadt*, the Court construed the "misrepresentation" exception to the Federal Tort Claims Act, 28 U.S.C. 2680(h), as barring suits against the United States for failure to discover and disclose defects in houses built with government financial assistance. This construction of the Tort Claims Act has been carefully respected by the lower courts for the past 20 years and has never been altered by Congress. Because the decision below is in utter disregard of the unambiguous holding in *Neustadt*, it is appropriate for the Court to grant this petition and reverse the Sixth Circuit's decision summarily.

1. In *United States* v. *Neustadt*, *supra*, plaintiffs purchased a home with a private mortgage loan insured by the Federal Housing Administration (FHA). Prior to issuing the insurance commitment, the FHA inspected the house and appraised its value for mortgage insurance purposes. When the foundation of the house subsequently proved to have cracks in it, plaintiffs sued the FHA under the Federal Tort Claims Act on the theory that it had breached a "duty to use due care in obtaining and communicating information upon which [the other] party may reasonably be expected to rely * * *." 366 U.S. at 706.

The court of appeals in *Neustadt* upheld a judgment in plaintiffs' favor, finding that the complaint alleged a claim for negligence and not misrepresentation, but this Court reversed. Looking behind the

language used in the complaint to determine the real basis for the claim, the Court held that plaintiffs alleged only "the traditional and commonly understood * * * tort of 'negligent misrepresentation,' " for which no recovery would lie under the Tort Claims Act. 366 U.S. at 706.

This Court thus recognized in *Neustadt* that Congress intended broadly to preclude suits against the United States for damages caused by misinformation or a failure to communicate information properly to the plaintiff. See *National Manufacturing Co.* v. *United States*, 210 F.2d 263, 276 (8th Cir.), cert. denied, 347 U.S. 967 (1954) (intent to except "cases where mere 'talk' or failure to 'talk' * * * is asserted"). The decision in this case is not faithful to that interpretation of the statute. Applying the *Neustadt* approach, the court of appeals should have looked beyond respondent's general allegations of negligence by the FmHA and recognized that the gravamen of respondent's complaint is that the government was negligent in not discovering the defects and disclosing their existence to her. Respondent does not allege, nor could she, that the government had the responsibility to build or rebuild the house.[5]

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[5] The purpose of the requirement of supervision and inspection in the 1949 Housing Act is the same as in the 1934 Act involved in *Neustadt*, *i.e.*, to protect the government's interest in the loan. Thus, the legislative history of the National Housing Act of 1949 clearly indicates that "[t]he extent of the requirements for building plans, supervision, and inspection would depend upon the character of the construction and the *amount of the loan.*" S. Rep. No. 84 (Pt. 2), 81st Cong., 1st Sess. 20 (1949) (emphasis added). See also H.R. Rep. No. 590, 81st Cong., 1st Sess. 12, 56 (1949); 95 Cong. Rec. 4764 (1949) (remarks of Sen. Langer).

Respondent's claim is correctly characterized by the authorities cited in *Neustadt* as one of negligent misrepresentation. Thus, the American Law Institute's *Restatement of Torts* § 552 (1938) (emphasis added) described the liability for failure "to exercise that care and competence in *obtaining* and communicating the *information* which its recipient is justified in expecting * * *." Similarly, Dean Prosser defined the tort as "[n]egligence in *obtaining information* or in making the representation * * *." W. Prosser, *Torts* § 87 (1941) (emphasis added). See *United States* v. *Neustadt*, *supra*, 366 U.S. at 706-707 n.16. FmHA failed to note the construction defects in the inspection forms it gave to respondent because it allegedly was negligent in failing to obtain that information. Thus, respondent's claim is one arising out of negligent misrepresentation and therefore is barred by Sectior 2680(h).[8]

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[8] The court of appeals' argument is not advanced by its conclusionary statement that Congress "intended [respondent] to be the beneficiary of the inspection and technical assistance offered by FmHA * * *" (App. C, *infra*, 17a). This is directly contrary to the court's own interpretation of the purpose of the inspection program conducted by the FmHA. In rejecting respondent's implied contract theory, the court recognized that "[n]one of these provisions include a clearly defined obligation on the part of FmHA running to [respondent] to perform any supervisory function * * *" (*id.* at 11a). Instead, the FmHA program—like the FHA program in *Neustadt* (366 U.S. at 707-708)—is designed solely to protect the government's security interest. See note 5, *supra*. Given this view of the statute as implemented through the regulations, it is difficult to understand how the court of appeals could conclude that Congress intended to create a duty cognizable in a tort action to protect respondent from defects in construction.

In its attempt to avoid the clear mandate of *Neustadt*, the court of appeals asserted (App. C, *infra*, 13a) that its decision was controlled instead by *Indian Towing Co.* v. *United States*, 350 U.S. 61 (1955), a decision the Court in *Neustadt* was careful to preserve. See 366 U.S. at 711 n.26. *Indian Towing* involved the Coast Guard's failure properly to maintain the beacon lamp in a lighthouse, which caused a vessel to run aground. As the Court in *Neustadt* noted, "[s]uch a claim does not 'arise out of * * * misrepresentation * * *.'" 366 U.S. at 711 n.26.

This case, however, is identical to *Neustadt*, and the distinction the Court recognized between *Neustadt* and *Indian Towing* is the reason respondent's suit should be barred. In *Indian Towing*, if the Coast Guard had maintained the lighthouse properly, that would have completely protected the plaintiff, and no additional act of communication would have been required. Here, by contrast, even if the FmHA had not been negligent in its inspection and had discovered the defects in the house, respondent's injury would still have occurred unless that information was conveyed to her. Thus, the basis for respondent's claim ultimately rests on a failure of the inspection document to disclose the existence of those defects. The inspector's approval was a representation to respondent that the house was without defects, and the injury she suffered was caused by that misrepresentation, not by the government's negligent inspection.

Prior to the Sixth Circuit's decision in this case, the courts of appeals have been careful to distinguish between the *Indian Towing* situation, where government operations directly cause an injury, and the *Neustadt* situation, where the injury is caused by the government's failure to obtain and supply accurate

information. Compare, *e.g.*, *Baroni* v. *United States*, 662 F.2d 287 (5th Cir. 1981), petition for cert. pending, No. 81-1326 (filed Jan. 12, 1982); *Reynolds* v. *United States*, *supra*; *City and County of San Francisco* v. *United States*, 615 F.2d 498 (9th Cir. 1980); *Preston* v. *United States*, 596 F.2d 232 (7th Cir.), cert. denied, 444 U.S. 915 (1979); *Somali Development Bank* v. *United States*, 508 F.2d 817, 821 (Ct. Cl. 1974); *Thompson* v. *United States*, 408 F.2d 1075, 1081 (8th Cir. 1969); and *Cenna* v. *United States*, 402 F.2d 168 (3d Cir. 1968), with *Ware* v. *United States*, 626 F.2d 1278 (5th Cir. 1980); and *Hall* v. *United States*, 274 F.2d 69 (10th Cir. 1959). The court below has blurred this clear distinction by focusing only on respondent's generalized claim of negligence as the basis for the suit, while ignoring the fact that respondent's injury (like the injury in *Neustadt*) was based on a negligent *misrepresentation*.

2. The court of appeals' decision not only muddies the clear waters that heretofore had surrounded the "misrepresentation" exception to the Federal Tort Claims Act, but also disregards the congressional scheme for remedying the injury about which respondent complains. Obviously, the first source of protection against construction of defective housing must be the private developer or builder. See 7 C.F.R. 1924.252. But Congress realized that not all builders will be able or willing to make amends for their faulty construction. Instead of allowing the injured home buyer to sue the federal government for the injury caused in part by the failure to discover defects during an inspection, however, Congress provided a discretionary administrative remedy. Thus, in 42 U.S.C. (Supp. II) 1479(c), Congress authorized the Secretary of Agriculture to grant relief to a buyer of a

new home constructed with FmHA loan assistance, if the house has "structural defects." In such a case the Secretary may correct the defects, pay for the cost to the buyer of correcting the defects, or purchase the house outright. 42 U.S.C. (Supp. II) 1497(c); 7 C.F.R. 1924.252.[7]

Congress enacted this provision in 1977 to give the Secretary of Agriculture essentially the same authority held by the Secretary of Housing and Urban Development (see 12 U.S.C. 1735b(b)) with respect to individuals who had purchased defective houses with FHA-insured loans. H.R. Rep. No. 95-236, 95th Cong., 1st Sess. 171-172 (1977). HUD's authority was first granted in 1964, just three years after *Neustadt*, when Congress decided to assist "distressed homeowners who, after relying upon FHA construction standards and inspections, find structural or other major defects in their properties purchased with FHA-insured loans." S. Rep. No. 1265, 88th Cong., 2d Sess. 5 (1964).

At the time Congress took this remedial action, it was intimately familiar with the *Neustadt* decision. In the hearings on the general problem of how to assist these borrowers, *Neustadt* was carefully discussed. Indeed, the General Counsel of the Housing and Home Finance Agency explained in a statement to the Senate Subcommittee that passage of the administrative remedy to correct structural defects would result in "no modification of the principles relied on in the *Neustadt* case" and would cause "no

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[7] Indeed, respondent sought such relief, but it was denied, presumably because the defects were not substantial (App. D, *infra*, 24a-25a). The decision of the Secretary to withhold administrative relief is not reviewable by the courts. 42 U.S.C. (Supp. II) 1479(c).

enlargement of rights under the Federal Tort Claims Act." *Payment of Claims for Defects in FHA Homes: Hearings Before a Subcomm. of the Senate Comm. on Banking and Currency*, 88th Cong., 1st Sess. 133-134 (1963). Thus, Congress enacted this administrative remedy in the wake of the *Neustadt* decision, and it deliberately chose to make this the exclusive remedy in *Neustadt*-type cases. See *Summers* v. *United States*, 510 F.2d 123, 125 (8th Cir.), cert. denied, 423 U.S. 851 (1975). In light of Congress' determination to provide discretionary administrative relief for persons such as respondent, rather than to amend the Federal Tort Claims Act, the court of appeals' modification of the clear rule in *Neustadt* is particularly indefensible.

3. If, contrary to our submission above, the Court should regard this case as inappropriate for summary reversal, we submit that the case nonetheless plainly warrants plenary review. As previously noted (see page 13, *supra*), the court of appeals' rationale cannot be squared with *Neustadt* or the numerous post-*Neustadt* decisions that have recognized the distinction between injuries caused by government *operations* based on misinformation and injuries caused by government *misrepresentations* based on misinformation. Moreover, the decision below is in direct conflict with two recent decisions of the Tenth Circuit based on virtually identical facts. In *Reynolds* v. *United States*, *supra*, and *Ortiz* v. *United States*, 661 F.2d 826, 829-930 (1981), the Tenth Circuit held that the United States is not liable under the Federal Tort Claims Act for damages caused by negligent FmHA inspections. Indeed, the court of appeals in this case acknowledged that the decision

in *Reynolds* "appears to be contrary to our holding" (App. C, *infra*, 18a n.7).[8]

Thus, it is necessary for the Court to resolve this conflict on an issue that may affect all governmental inspection programs, in order to clarify the extent of the government's exposure to monetary liability in this recurring class of cases.[9]

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[8] The court of appeals stated that in *Reynolds* the injury involved was a personal injury to an invitee of the owner of the FmHA-financed house, and hence that the injury was not "direct" (App. C, *infra*, 18a n.7). But the Tenth Circuit did not decide the case on causation grounds, and thus this difference does not alter the conflict that exists between the two courts of appeals. Moreover, *Ortiz* (which reached the same conclusion as *Reynolds*) involved property damage directly suffered by the home buyer rather than an injury to a third party.

[9] We note that the government's potential liability under the FmHA program could be quite substantial. The Department of Agriculture informs us that in 1980 alone the FmHA closed 90,000 loans involving inspections similar to those at issue in this case. In addition, the court of appeals' decision already has been followed by at least one district court. See *Park* v. *United States*, 517 F. Supp. 970 (D. Ore. 1981), appeal docketed, No. 81-3524 (9th Cir. Dec. 11, 1981). See also Petition for a Writ of Certiorari, *Baroni* v. *United States*, No. 81-1326 (filed Jan. 12, 1982) (alleging a conflict between the decision below and *Baroni* v. *United States*, 662 F.2d 287 (5th Cir. 1981)).

CONCLUSION

The petition for a writ of certiorari should be granted and the judgment of the court of appeals reversed summarily on the authority of *United States* v. *Neustadt*, 366 U.S. 696 (1961).

Respectfully submitted.

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FEBRUARY 1982

Appendix

APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

No. 80-1278

ONILEA NEAL, PLAINTIFF-APPELLANT

v.

ROBERT BERGLUND [*sic*], ET AL.,
DEFENDANTS-APPELLEES

[Filed Sep. 28, 1981]

Before: MERRITT and MARTIN, Circuit Judges; COHN, District Judge.*

ORDER

A majority of the active judges of this court having failed to request that a vote be taken on the suggestion that the petition for rehearing be heard en banc, the petition was referred by the Chief Judge of this court to the panel for determination.

Upon consideration, it is ordered that the petition for rehearing be and is denied.

ENTERED BY ORDER OF THE COURT

/s/ John P. Hehman
Clerk

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* The Honorable Avern Cohn, Judge, U.S. District Court for the Eastern District of Michigan, sitting by designation.

APPENDIX B

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

No. 80-1278

ONILEA NEAL, PLAINTIFF-APPELLANT

vs.

ROBERT BERGLAND, ET AL., DEFENDANTS-APPELLEES

[Filed May 1, 1981]

Before: MERRITT and MARTIN, Circuit Judges; COHN, District Judge.

JUDGMENT

Appeal from the United States District Court for the Eastern District of Tennessee

THIS CAUSE came on to be heard on the record from the United States District Court for the Eastern District of Tennessee and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court in this cause be and the same is hereby reversed and the case re-

manded for further proceedings consistent with the opinion filed today.

No costs taxed.

ENTERED BY ORDER OF THE COURT

/s/ John P. Hehman
Clerk

A True Copy.

Attest:

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Deputy Clerk

Issued as Mandate:

APPENDIX C

UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

No. 80-1278

ONILEA NEAL, PLAINTIFF-APPELLANT

v.

ROBERT BERGLAND, ET AL., DEFENDANTS-APPELLEES

Appeal from the United States District Court
Eastern District of Tennessee

Decided and Filed May 1, 1981

Before: MERRITT and MARTIN, Circuit Judges; COHN, District Judge.*

I.

COHN, District Judge. Plaintiff appeals from a dismissal of her action against Robert Bergland, Secretary of Agriculture, and others,[1] for failure to

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* Honorable Avern Cohn, United States District Judge, Eastern District of Michigan, sitting by designation.

[1] Other defendants are Gordon Cavanaugh, Administrator of the Farmers Home Administration; Earl Wayne Avery, Tennessee State Director of the Farmers Home Administration; S. Lane Parkison, Roane County Supervisor of the Farmers Home Administration; Mary C. Wells, Assistant Roane County Supervisor of the Farmers Home Administration; Home Marketing Associates, Inc., a construction com-

state a claim upon which relief can be granted and for lack of subject matter jurisdiction. The District Court, in a decision reported at 489 F. Supp. 512 (E.D. Tenn. 1980), held that neither Title V of the Housing Act of 1949 (the Act), 42 U.S.C. § 1471 *et seq.*, nor regulations issued thereunder, 7 C.F.R. § 1802.71 *et seq.*, create an obligation on the part of the Farmers Home Administration (FmHA)[2] to supervise, inspect or warrant the construction of the prefabricated house built for plaintiff by defendant Home Marketing Associates (Home Marketing) and financed by FmHA.

For the reasons that follow we reverse and remand for further proceedings.

II.

Plaintiff is an unmarried woman in her mid-fifties with less than a high school education. She has never before owned a home. After an unsuccessful attempt to find housing to rent or purchase within her financial means, plaintiff applied for and received a direct rural housing loan from FmHA in 1976.

Plaintiff then consulted with defendant Parkison and entered into a construction contract with defendant Home Marketing for the construction of a prefabricated house. The contract provided that construction conform to FmHA approved plans; that

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pany; and C. E. Scott, Jr., Gary Humphreys and Wayne Humphreys, employees of or doing business as Home Marketing Associates, Inc.

[2] FmHA is an agency of the Department of Agriculture authorized by § 502 of Title V of the Housing Act of 1949, 42 U.S.C. § 1472, to extend financial assistance in home construction and purchase to persons of low to moderate income residing in rural areas.

changes in the plans be made only with the written approval of FmHA; and that FmHA have the right to inspect or test all materials and workmanship and reject any that were defective.

During the course of construction, defendant Wells conducted inspections of the house when it was 2% complete, 99% complete and 100% complete. There were no notes or comments in any of her inspection reports indicating any condition at variance with the approved plans and specifications.

Upon completion of construction, defendant Home Marketing issued plaintiff a one year builder's warranty as required by FmHA, which represented construction was in conformance with the drawings and specifications approved by FmHA and the minimum property standards published by the Department of Housing and Urban Development. The warranty covered workmanship, materials and equipment including the heating system.

In December 1977 plaintiff notified FmHA and defendant Home Marketing that the heat pump in her house was not working properly. Defendant Avery and other FmHA officials inspected the house and notified defendant Home Marketing of thirteen defects, including the heat pump, which needed correction. Defendant Home Marketing failed to cure the defects.

In November 1978 plaintiff asked FmHA to pay for correcting the heating system and other construction defects. It declined. After exhausting her administrative remedies, 28 U.S.C. § 2675, plaintiff brought this suit.

III.

The case was started in the Circuit Court of Roane County, Tennessee and thereafter removed to the

United States District Court for the Eastern District of Tennessee by defendant Bergland. 28 U.S.C. § 1441.

In her amended complaint plaintiff alleged a breach of contract by FmHA for failure to provide technical assistance including inspection and supervision of construction of the house; negligence for failure to properly execute its obligation to inspect and supervise construction of the house; and detrimental reliance for failure to perform its regulatory obligations as promised. Plaintiff also sought mandamus to compel defendant Bergland to compensate her for the construction defects in the house under Section 509 of the Act, 42 U.S.C. § 1479(c).[3]

In essence, plaintiff alleged the Act and the regulations under it created an obligation on the part of FmHA to supervise construction of the house to ensure compliance with the purpose of the FmHA loan program which the Act recites is for rural residents to obtain "decent, safe, and sanitary living conditions . . . ." 42 U.S.C. § 1471(a).

The District Court rejected plaintiff's claims and remanded the case to the state court holding there is no duty owed plaintiff by FmHA under the Act since the purpose of the rural housing loan program is limited to providing participants with an opportunity to obtain decent housing and not to make the government "an insurer of the quality of the workmanship or structures funded with the loan proceeds." 489 F. Supp. at 514. The District Court equated FmHA's position with that of a mortgagee and looked at supervision of construction authorized

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[3] At oral argument plaintiff represented defendant had satisfied this request thereby mooting this issue.

by the regulations as a means of protecting FmHA's security interest in the mortgaged property.

> "To hold the FmHA liable for the shoddy work of the contractor would be tantamount to making a mortgagee the warrantor of the quality of its security."

489 F. Supp. at 515.

IV.

A.

The Secretary of Agriculture is authorized by § 502 of the Act, 42 U.S.C. § 1472, to extend financial and technical assistance, through FmHA, to eligible rural residents to enable them to obtain "decent, safe, and sanitary" housing. 42 U.S.C. § 1471(a). The regulations state,

> "The basic objective of the Farmers Home Administration (FmHA) in making section 502 loans is to assist farmowners and other persons who will live in rural areas to obtain decent, safe, and sanitary dwellings and related facilities. The purpose of these loans is to give families, who do not have sufficient resources to provide such dwellings and related facilities on their own account and cannot obtain the necessary credit from other sources on terms and conditions they reasonably can be expected to meet, an opportunity to have adequate homes."

7 C.F.R. § 1822.2.

FmHA is authorized to provide financial assistance either by direct loans through the Secretary of Agriculture pursuant to section 502 of the Act, 42 U.S.C. § 1472, or by insured or guaranteed loans

pursuant to section 517 of the Act, 42 U.S.C. § 1487, and the regulations, 7 C.F.R. § 1841.46 *et seq.*

Although Title V focuses on financial assistance, S. Rep. No. 84, 81st Cong., 1st Sess. 2, *reprinted in* [1949] U.S. Code Cong. Serv. 1550, 1576, Congress has also provided for research and technical services "pointed toward more efficient and more economical construction" of homes and related structures. *Id.* Section 506 of the Act provides,

> "Buildings and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary. In addition to the financial assistance authorized . . . *the Secretary is authorized to furnish . . . technical services such as building plans, specifications, construction supervision and inspection . . . .*"

42 U.S.C. § 1476(a) (emphasis added).

The regulations provide:

> "Supervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect the interests of the Government . . . ."

7 C.F.R. § 1822.7(a).

Thus while it may be said that the overall objective of the loan program is to provide rural residents an opportunity for decent, safe, and sanitary housing, it is to be noted that Congress has specifically authorized FmHA to provide technical assistance and supervision of construction.

B.

Plaintiff's contract claim turns on the nature and extent of FmHA's obligation, if any, to provide tech-

nical assistance and to inspect and supervise construction. To find FmHA had a contractual obligation it must be expressly provided for either in the Act, the regulations, or the loan papers, or it must be implied in fact from the circumstances surrounding plaintiff's dealings with FmHA, since there can be no right of action against the United States for a contract implied in law. 28 U.S.C. § 1346;[4] *Goodyear Tire & Rubber Co.* v. *United States*, 276 U.S. 287, 293 (1928).

There is no allegation that FmHA expressly promised to provide assistance and neither in the Act nor the regulations is there an explicit obligation on the part of FmHA to inspect or supervise construction for plaintiff's benefit. The right to inspect, without more does not imply an obligation to inspect. *Kaminer Construction Corp.* v. *United States*, 488 F.2d 980 (Ct. Cl. 1973).

Section 506 of the Act, 42 U.S.C. § 1476(a), authorizes the Secretary of Agriculture to furnish a borrower technical services; the regulations governing rural housing loans, 7 C.F.R. § 1822.7, provide that such assistance will be rendered "to the extent

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[4] The Tucker Act, 28 U.S.C. § 1346, governs contract actions against the United States. It provides,

> "(a) The district courts shall have original jurisdiction, concurrent with the Court of Claims, of:
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> * * * *
>
> (2) Any other civil action or claim against the United States not exceeding $10,000 in amount, founded . . . upon any express or implied contract with the United States . . . ."

This section acts as a waiver of sovereign immunity and therefore allows the United States to be sued in contract. *Tempel* v. *United States*, 248 U.S. 121, 129 (1918); *National Bank of Newark* v. *United States*, 357 F.2d 704, 706 (Ct. Cl. 1966).

necessary" to achieve the loan objectives; 7 C.F.R. § 1804.4(g)(3), governing planning and performing development work, provides that inspections will be made "as frequently as necessary to assure that construction and land development conforms with the plans and specification"; and 7 C.F.R. § 1802.73 and § 1802.74, governing supervision of borrowers, provide for "supervision necessary to accomplish the objectives of the loan," with emphasis given to, *inter alia*, maintaining the security and protecting the interest of FmHA. Borrowers are to be supervised "to the extent necessary to assure . . . protection of the FmHA's financial interest." 7 C.F.R. § 1802.74. None of these provisions include a clearly defined obligation on the part of FmHA running to plaintiff to perform any supervisory function, but instead speak in terms of discretion on the part of FmHA to render such assistance as it deems necessary to achieve the objectives of the loan program and for the protection of its security interest.

We find that no contractual obligation existed on the part of FmHA to provide technical assistance or to supervise construction or to inspect. *See Ramsey* v. *Farmers Home Administration*, 443 F. Supp. 760 (E.D. Mo. 1978); *Adamsville Lumber Co., Inc.* v. *Rainey*, 348 F. Supp. 373 (W.D. Tenn. 1972); *Forcum-Lannon, Inc.* v. *Berry*, 344 F. Supp. 774, (W.D. Tenn. 1972).

C.

Plaintiff's tort claim, however, is on firmer ground; namely the principle expressed in § 323 of the RESTATEMENT (SECOND) OF TORTS (1965)[5] that one

[5] RESTATEMENT (SECOND) OF TORTS § 323 provides:

"One who undertakes, gratuitously or for consideration, to render services to another which he should recognize

who undertakes to act, even though gratuitously, is required to act carefully and with the exercise of due care and will be liable for injuries proximately caused by failure to use such care. The Federal Tort Claims Act, 28 U.S.C. § 2671 *et seq.*, authorizes suit against the United States for this kind of claim since the act constitutes a waiver by the United States of its immunity from liability in tort for the acts of its employees and representatives. *Reminga* v. *United States*, 631 F.2d 449 (6th Cir. 1980); Annot., 30 A.L.R. Fed. 421, 430 (1976). This act makes the United States liable, with certain exceptions, 28 U.S.C. § 2680, for the negligence of its employees "in the same manner and to the same extent as a private individual under like circumstances . . . ." 28 U.S.C. § 2674.

The principle expressed in the Restatement is not new, *Erie R. Co.* v. *Stewart*, 40 F.2d 855 (6th Cir. 1930), and has been applied in a number of situations in which a government agency performed the undertaking. *Ingham* v. *Eastern Air Lines, Inc.*, 373 F.2d 227 (2d Cir.), *cert. denied*, 389 U.S. 931 (1967), for example, deals with a negligent act occurring in the operation of the federal air traffic control system.

> "It is now well settled that when the government undertakes to perform services, which in

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as necessary for the protection of the other's person or things, is subject to liability to the other for physical harm resulting from his failure to exercise reasonable care to perform his undertaking, if

(a) his failure to exercise such care increases the risk of such harm, or

(b) the harm is suffered because of the other's reliance upon the undertaking."

> the absence of specific legislation would not be required, it will, nevertheless, be liable if these activities are performed negligently. Thus, for example, though the government may be under no obligation in the absence of statute to render medical care to discharged veterans, when it decides to provide such services and does so negligently, it has been held liable under the Tort Claims Act. *United States* v. *Brown*, 348 U.S. 110, 75 S.Ct. 141, 99 L.Ed. 139 (1954)."

373 F.2d at 236.

In *Indian Towing Co.* v. *United States*, 350 U.S. 61 (1955), this principle was applied to the Coast Guard in a situation where it was charged with failure to maintain the beacon lamp in a lighthouse resulting in damage to a barge that went aground. The Supreme Court said that while the Coast Guard need not have undertaken the lighthouse service, once it exercised its discretion to operate the light, thereby engendering reliance on the guidance afforded by the light, it was obligated to use due care to maintain the light and to make repairs or give warnings when the light was not functioning. For failure to do so it was liable in money damages for any injury which resulted.

The government has been held liable for the negligence of its employees in the way they put out a forest fire, *Rayonier, Inc.* v. *United States*, 352 U.S. 315 (1957); for the negligent design and construction of a drainage ditch which caused damage to a railroad, *Seaboard Coast Line Railroad Co.* v. *United States*, 473 F.2d 714 (5th Cir. 1973); for negligence of the Coast Guard in undertaking a rescue operation, *United States* v. *DeVane*, 306 F.2d 182 (5th Cir. 1962); for negligence in inaccurately marking

the location of a wrecked ship, *Somerset Seafood Co.* v. *United States*, 193 F.2d 631 (4th Cir. 1951); and for negligence in failing to require a subcontractor to comply with a contract's safety requirements, *Barron* v. *United States*, 473 F. Supp. 1077 (D. Hawaii 1979).

V.

Where claims for negligence against the government have been barred by the Federal Tort Claims Act, *United States* v. *Neustadt*, 366 U.S. 696 (1961) and its progeny, circumstances different than the case at bar were involved.

In *Neustadt*, plaintiffs purchased a house with a private mortgage loan insured by the Federal Housing Administration (FHA) pursuant to § 203 of the National Housing Act of 1934, 12 U.S.C. § 1709. In determining whether the house was eligible for FHA mortgage insurance, the FHA made an inspection and assigned an appraised value to establish the maximum amount of mortgage insurance obtainable. 24 C.F.R. §§ 200.140 - 200.152. FHA found no defects in the house and issued an insurance commitment. Pursuant to § 226 of the National Housing Act of 1934, 12 U.S.C. § 1715q, the seller provided plaintiffs with a copy of the appraisal report.

Shortly after plaintiffs took possession, the foundation of the house began to shift causing substantial damage to interior and exterior walls. Plaintiffs sued FHA claiming it negligently inspected and appraised the house. Plaintiffs sought recovery of the difference between the fair market value and the purchase price paid claiming they relied on the excessive FHA appraisal.

The Supreme Court denied plaintiff's recovery on the grounds the purpose of the FHA appraisal program is the " 'protection of the Government and its insurance funds' ", 366 U.S. at 709, and that any tort committed by FHA because of an inaccurate report resulting from negligent inspection of the house, would be one "arising out of . . . misrepresentation" a specie of claims which is specifically excluded from coverage by the Federal Tort Claims Act, 26 U.S.C. § 2680(h).[6]

> "[T]he duty to use due care in obtaining and communicating information upon which that party may reasonably be expected to rely in the conduct of his economical affairs, is only to state the traditional and commonly understood legal definition of the tort of 'negligent misrepresentation'. . . ."

366 U.S. at 706. *See also United States* v. *Lawrence Towers, Inc.*, 236 F. Supp. 208 (E.D.N.Y. 1964).

Examples of *Neustadt* type situations are *Green* v. *United States*, 629 F.2d 581 (9th Cir. 1980), involving a suit by cattle owners against the United States for losses sustained from the application of DDT to cattle grazing land and the failure to adequately warn of the consequences of the chemical; *Preston* v. *United States*, 596 F.2d 232 (7th Cir.

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[6] "The provisions of this chapter and section 1346(b) of this title shall not apply to—

* * * *

(h) Any claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit or interference with contract rights . . . ."

28 U.S.C. § 2680(h).

1979), involving a suit by farmers against the United States for losses sustained as a result of storing grain in a warehouse approved by the Department of Agriculture which went bankrupt; and *Marival, Inc.* v. *Planes, Inc.*, 306 F. Supp. 855 (N.D. Ga. 1969), involving a third-party action by the seller of an airplane against the United States for the negligent certification of airworthiness of the airplane given by the Federal Aviation Administration which caused the seller to misrepresent the condition of the plane to the buyer.

Cases distinguishing *Neustadt* illustrate the difference between the application of the Federal Tort Claims Act to a situation dealing with a cause of action based on misrepresentation and a cause of action based on negligent performance of an operational task. In *Ware* v. *United States*, 626 F.2d 1278 (5th Cir. 1980), the negligent misrepresentation exception was held inapplicable to a suit by a farmer against the United States for losses sustained when the Government destroyed his cattle after the Department of Agriculture negligently misdiagnosed them as tubercular.

> "The government's misrepresentation caused Ware to do nothing save remain in ignorance that he had suffered a compensable loss. The government[,] not Ware, destroyed the cattle and caused the damage. Ware's complaint, thus, arose out of, not a negligent misrepresentation, but an allegedly negligent misdiagnosis that caused the government to destroy his cattle."

626 F.2d 1283.

In *In Re Air Crash Disaster Near Silver Plume Colo.*, 445 F. Supp. 384 (D. Kan. 1977), there was a

claim of negligent failure on the part of a government employee to perform an operational duty to properly inspect an aircraft. The District Court held,

> "It is the inspection undertaken to protect air travelers from certain dangers which is relied upon by such travelers and which, if negligently performed, gives rise to the very dangers the inspection was intended to prevent. The certification is a reporting of results of such inspection but was not in itself relied upon by plaintiffs in any economic affairs."

445 F. Supp. at 409.

VI.

Plaintiff's claim, as we read it, is based not on misrepresentation, as in the issuance of a false or inaccurate appraisal report, but rather on FmHA's failure to use due care in a voluntary undertaking, i.e., inspection and supervision of the construction of her house. Congress, we believe, intended plaintiff to be the beneficiary of the inspection and technical assistance offered by FmHA given the purpose of the Act and plaintiff's particular circumstances.

The Supreme Court in *Neustadt* noted the distinction we make that its decision "neither conflicts with nor impairs" the authority of *Indian Towing Co.* v. *United States, supra*, saying:

> "As Dean Prosser has observed, many familiar forms of negligent conduct may be said to involve an element of 'misrepresentation,' in the generic sense of that word, but '[s]o far as misrepresentation has been treated as giving rise in and of itself to a distinct cause of action in tort, it has been identified with the common law

> action of deceit,' and has been confined 'very largely to the invasion of interests of a financial or commercial character, in the course of business dealings.' Prosser, Torts, § 85, 'Remedies for Misrepresentation,' at 702-703 (1941 ed.). See also 2 Harper and James, Tort, § 29.13, at 1655 (1956)."

366 U.S. at 711, n. 26.

There is nothing in the amended complaint or in the facts and circumstances here present which lead to the conclusion that the kind of misrepresentation, as was found in *Neustadt* and as is specifically excluded under § 2680(h) of the Federal Tort Claims Act, is the basis of plaintiff's claim. What plaintiff is complaining of is that FmHA negligently supervised construction and negligently inspected her house.

VII.

The District Court erred in dismissing the amended complaint. It does not appear beyond doubt "that plaintiff can prove no set of facts in support of [her] claim which would entitle [her] to relief." *Conley* v. *Gibson*, 355 U.S. 41, 45 (1957). The judgment of the District Court is REVERSED and this cause REMANDED to the District Court for further proceedings consistent with this opinion.[7]

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[7] Subsequent to the decision in this case the Court of Appeals for the Tenth Circuit released its opinion in *Reynolds, et al.* v. *United States*, No. 79-2068 (filed March 9, 1981), which appears to be contrary to our holding above. Careful review suggests that we take a different view of Congressional intent and the purposes of the statute with regard to technical assistance. Here, unlike *Reynolds*, the damages claimed were the direct consequences of the alleged negligent inspections, i.e., defects in the house. We are satisfied that plaintiff is entitled to go forward with her case.

APPENDIX D

UNITED STATES DISTRICT COURT
E. D. TENNESSEE, N. D.

Civ. No. 3-80-36

ONILEA NEAL

v.

ROBERT BERGLAND, SECRETARY
OF AGRICULTURE, ET AL.

Feb. 26, 1980

MEMORANDUM

ROBERT L. TAYLOR, District Judge.

Plaintiff filed this action in the Circuit Court of Roane County, Tennessee, claiming damages arising out of the defective construction of a prefabricated home financed by a loan from the Farmers Home Administration (FmHA). Because several federal officials were named as party defendants, the United States Attorney removed the case to this Court pursuant to 28 U.S.C. § 1442. Subsequently, a Rule 12 (b) motion was filed to dismiss the federal defendants for lack of subject matter jurisdiction and for failure of plaintiff to state a claim upon which relief can be granted. That motion is currently before this Court.

For the purposes of this motion, we shall accept as true the facts alleged in the complaint. Plaintiff avers that in August, 1976, she applied for a Rural Housing Loan with FmHA in Roane County, Tennessee, which loan was approved on or about June 9,

1977. FmHA is an agency under the auspices of the Department of Agriculture authorized to make such loans by § 502 of Title V of the Federal Housing Act of 1949, as amended. 42 U.S.C. § 1472. Shortly after the loan was approved, plaintiff entered into a contract with defendant Home Marketing Associates for the purchase and construction of a prefabricated home on a small lot she had recently purchased. Home Marketing warranted that it would install a "General Electric . . . 220 Volt . . . 15 kw Btuh" heating system. There are in addition some 13 other defects specified in the complaint.

Plaintiff further alleges that while this house was being built, the structure was inspected three times by a representative of FmHA. She says that because the representative failed to note the alleged defects and deviations from the plans, the house is of substandard quality and she has been damaged.

Plaintiff claims that both Home Marketing and the FmHA, and its representatives, are liable to her for the amount of damages she has sustained. She proceeds for damages against FmHA on three theories: to wit, breach of contract, negligence, and detrimental reliance. In addition, by an amended complaint, plaintiff seeks mandamus to compel the Secretary of Agriculture to "pay or otherwise compensate plaintiff" for the construction defects in her dwelling. We shall address these theories in order. In doing so, of course, we express no opinion about the merits of plaintiff's claim against the non-federal defendants.

(1) *Breach of Contract*

Plaintiff alleges that under the regulation and statute, and by the terms of the loan commitment, promissory notes, and deed of trust, the FmHA has

in effect "promised to provide plaintiff technical assistance including inspection and supervision of the construction of plaintiff's new home and to insure [sic] that the provisions of the contract were fulfilled." (Amended complaint, ¶ 30)

A thorough review of the cited documents reveals no such express promises. The issues raised by plaintiff's claim are therefore (1) whether the statute and regulations are incorporated within those documents, and (2) if so, whether they create on the part of the FmHA a duty *to plaintiff* to supervise the construction of the structure.

Plaintiff relies on regulations promulgated by the Secretary providing that the County Supervisor (the relevant FmHA representative) must inform the borrower and the payee that loan money will be released only if "the quality and quantity of items purchased are in accordance with approved plans" (7 CFR § 1803.7(d)(3)(i)), and that the amount due the builder will be paid only if the work is in compliance "with all items and conditions of the contract" (7 CFR § 1804.4(d)(7)(vii)(a)). Plaintiff argues that the provision of 7 CFR § 1822.7(a) together with 7 CFR § 1822.2 also create a duty *to plaintiff* to supervise the building of her structure, for the breach of which the FmHA is liable.

We cannot agree. 7 CFR § 1822.7(a) provides:

> Supervision will be provided borrowers to the extent necessary to achieve the objectives of the loan *and to protect the interests of the Government* . . . . (Emphasis added)

The basic objectives of the FmHA program are enunciated in 7 CFR § 1822.2:

> The basic objective of the Farmers Home Administration (FmHA) in making Section 502 loans is to assist farmowners and other persons who will live in rural areas to obtain decent, safe, and sanitary dwellings and related facilities. The purpose of the loan is to give families, who do not have sufficient resources to provide such dwellings and related facilities on their own account and cannot obtain the necessary credit from other sources on terms and conditions they can reasonably expect to meet, *an opportunity* to have adequate homes. (Emphasis added.)

It is clear that in making these loans available to low-income rural inhabitants, the government sought only to provide them with an *opportunity* to obtain decent housing not otherwise open to them in the private sector. The government did not intend to make itself an insurer of the quality of the workmanship or structures funded with the loan proceeds.

As a condition of making a loan, the FmHA must perfect a security interest in the dwelling built or purchased, 7 CFR § 1822.10, and the amount of the loan is limited by the market value of that security. 7 CFR § 1822.7(3). Thus, the FmHA assumes the position of a mortgagee of the property. It follows that the government would have a strong interest in ensuring that the value of its security would remain adequate to cover the balance of the loan in the event of default by the borrower, especially in view of the risks inherent in the program. The supervision of the building process mandated by the regulations serves this function, and, as the government argues, any benefit to the borrower is purely incidental. In fact, the regulation calling for final inspection by the County Supervisor provides that he should be "ac-

companied by the borrower when practicable." 7 CFR § 1804.4(g)(1).

To hold the FmHA liable for the shoddy work of the contractor would be tantamount to making a mortgagee the warrantor of the quality of its security. Plaintiff has cited no authority for this proposition, nor have we found any.

The Court holds that even if the regulations are incorporated into the loan obligation agreement between plaintiff and FmHA, they create no duty running from FmHA *to plaintiff* to warrant the quality of the structure purchased with the loan proceeds. See *Ramsey* v. *Farmers Home Administration*, 443 F.Supp. 760 (E.D. Mo. 1978). Accordingly, plaintiff's first cause of action must be dismissed as against the government.

(2) *Negligence*

Plaintiff's second claim based on negligence is likewise premised on the duties imposed on FmHA by the regulations. Plaintiff claims that FmHA and its employees breached their duty to supervise and inspect the building of plaintiff's dwelling. We have already held that the regulations create no duty running to plaintiff. Therefore, there can be no actionable breach of such duty. Accordingly, plaintiff has here, too, failed to state a claim as against the government defendants.

(3) *Detrimental reliance*

Plaintiff's third claim styled "detrimental reliance" must also fail. Plaintiff says that "during the course of the entire transaction" defendant employees of the FmHA "promised to perform their regulatory duties" to supervise construction and "to oversee the relation-

ship between the contractor and the plaintiff," and that these promises induced her to *enter into* the contracts with Home Marketing and the FmHA (Amended Complaint, ¶¶ 36, 37, 39.)

In order to state a claim, plaintiff must allege that the promises actually *induced* her to take "action . . . of a definite and substantial character." Rest.2d Contracts, § 90. The action induced was *entering into* the contracts with Home Marketing and FmHA. It appears from the face of the complaint, however, (at ¶ 36) that the alleged promises were made only "during the course of the . . . transaction." Thus, the promises complained of, having apparently been made only *after* plaintiff entered into the contracts, could not have induced her to act.

In any event, in view of our interpretation of the regulations, and those of other courts (see, *e.g.*, *Adamsville Lumber Co., Inc.* v. *Rainey*, 348 F.Supp. 373, 377 (W.D. Tenn. 1972); *Ramsey* v. *Farmers Home Administration*, 433 F.Supp. 760 (E.D. Mo. 1978)), a promise by employees of FmHA "to perform their regulatory duties" (Amended Complaint, ¶ 36) could not reasonably have been expected to induce plaintiff to enter into the said contracts. Rest. 2d, Contracts ¶ 90.

(4) *Mandamus*

In her amended complaint, plaintiff has added a cause of action seeking mandamus compelling the Secretary to "pay or otherwise compensate" her for construction defects in her dwelling. The Secretary's alleged duty in this regard is premised on 42 U.S.C. § 1479(c), and regulations promulgated thereunder, 7 CFR § 1924.251 *et seq.*, which authorize payment

by the Secretary to the owner for defective construction.

The claim must fail for three reasons. First 7 CFR § 1924.251 states:

> Provisions of this subpart do not apply to dwellings financed through the guaranteed Section 502 program.

Our research has revealed no reason to believe that the loan in question does not fall within this exemption.

Secondly, § 1924.252 states, in part:

> If a complaint is justified and covered by the provisions of the builder's warranty, the *builder* is expected to make the necessary corrections. (Emphasis added.)

Since the alleged defects appear to be covered by the builder's warranty, they are his responsibility, not that of the FmHA. In any event, the section continues:

> [T]he cost for repairing structural defects, in newly constructed dwellings not corrected by the builder *may* be paid by the government, or the borrower *may* be compensated for repairing such defects under the provisions of this subpart. (Emphasis added.)

It is clear from the wording of the regulation that compensation lies wholly within the discretion of the Secretary or his designee. As such there is simply no basis on which this Court can order payment.

Finally, a reading of the regulation reveals that its purpose is to authorize either direct payment for repair of the defects or *reimbursement* to the owner for expenditures she has made. There is no allegation

in the complaint that plaintiff has expended any of her own money in an effort to repair the alleged defects. To order payment of compensation without such prior payment would be tantamount to ordering the FmHA to pay damages to plaintiff, the basis for which this Court has already held in this opinion to be non-existent. Plaintiff cannot get indirectly that to which she is not entitled directly.

For the above reasons, this Court is of the opinion that plaintiff has failed to state facts upon which relief from the government defendants can be based. As pointed out above, we express no opinion with regard to her claims against Home Marketing and the other private defendants. It shall accordingly be ordered that the government be dismissed from this case. Since such action destroys this Court's jurisdiction based on 28 U.S.C. § 1346(b), and no other bases of jurisdiction have been alleged as to the remaining defendants, it shall also be ordered that the case be remanded to the Circuit Court of Roane County, where it was originally brought.

But we feel we must make two final observations. Fed.R.Civ.P. 8(a) prescribes the general requirements for a complaint filed in federal court. Paramount among these is that the complaint contain "a *short and plain* statement of the claim . . . ." With some exceptions, the purpose of the pleading is to apprise the opposition of the facts giving rise to the complaint and to put him on notice of the nature of the action against which he must defend. The complaint is *not* the proper place for legal argument. Yet in the instant case, the 19-page pleading is virtually packed with statutory and regulatory citations, and portions of no less than six such provisions are set out verbatim—some virtually in their

entirety. While we respect the thoroughness of counsel's research, we are constrained to add that the inclusion of such minute detail in the initial pleading renders its review tedious and confusing. A short and plain statement of the claim is all that is needed.

Secondly, in his brief responding to the government's motion to dismiss, plaintiff cited several unreported decisions of the courts. Local Rule 11(b) provides, "Authorities not readily available to the Court . . . shall be supplied to the Court either in the original, or in legible, duplicate form." This was not done in this case, and the Court was forced to specifically request counsel to provide those opinions. This requires unnecessary delay, and we strongly urge that it not happen again. Fortunately, in the interests of plaintiff, the Court was able to put off its final decision until those opinions were supplied, but counsel should be assured that this Court has no intention of making such delay a common-place practice.

Order Accordingly.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1981 383748 751

Joint Appendix

Office - Supreme Court, U.S.
FILED
AUG 6 1982
ALEXANDER L. STEVAS.
CLERK

No. 81-1494

In the Supreme Court of the United States

OCTOBER TERM, 1981

JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET AL.,
PETITIONERS

v.

ONILEA NEAL

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

JOINT APPENDIX

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Solicitor General
Department of Justice
Washington, D.C. 20530
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PETITION FOR WRIT OF CERTIORARI FILED FEBRUARY 9, 1982
CERTIORARI GRANTED MAY 24, 1982

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IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF TENNESSEE

ONILEA NEAL

v.

ROBERT BERGLAND, SECRETARY OF AGRICULTURE, ET AL.

Docket Entries

Date	Proceedings
1980	
1-31	PETITION FOR REMOVAL from Circuit Court of Roane County, filed
1-31	NOTICE of filing of petition for removal, filed. C/S
2-5	MOTION TO DISMISS by defendants.
2-12	ENTRY OF APPEARANCE filed. C/S
2-12	NOTICE OF DEPOSITION upon oral examination & request for production of documents, filed. C/S
2-12	AMENDMENT to complaint, filed. C/S
2-12	AMENDED COMPLAINT filed. C/S
2-12	REQUEST FOR ORAL ARGUMENT filed. C/S
2-12	MEMORANDUM BRIEF in opposition to motion to dismiss, filed. C/S
2-21	REQUEST FOR ADMISSIONS plaintiff, filed. C/S
2-21	REQUEST FOR ADMISSIONS plaintiff, filed. C/S
2-21	MOTION for leave to proceed in forma pauperis & supporting affidavit, filed.
2-26	MEMORANDUM RL Taylor, DJ, dismissing all federal defendants and remanding case to the Circuit Court of Roane County, filed. C/M
2-26	ORDER on Memorandum, filed. Certified copy to Roane County by Clerk, C/M
2-26	ORDER that motion for pauper's oath is moot, filed. C/M
2-27	DEPOSITION of Wayne Humphreys, filed.
2-29	NOTICE of filing of deposition, filed. C/S
3-7	NOTICE of filing of depositions, filed. C/S
3-7	DEPOSITION of Mary C. Wells, filed.
3-7	DEPOSITION of S. Lane Parkison, filed.
4-11	MOTION for leave to appeal in forma pauperis & supporting affidavit, filed. C/S

4-11	ORDER allowing plaintiffs to appeal in forma pauperis filed. C/M
4-11	NOTICE OF APPEAL filed. Certified copies to U.S.A. and Mr. Ellis by Clerk.
4-11	Certified record on appeal mailed to the Court of Appeals for the Sixth Circuit.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF TENNESSEE
NORTHERN DIVISION

No. Civ 3–80–36

ONILEA NEAL, PLAINTIFF,

v.

ROBERT BERGLAND, SECRETARY OF AGRICULTURE, ET AL., DEFENDANTS.

AMENDED COMPLAINT

Introduction

1. This is an action for damages suffered by plaintiff by reason of a breach of contract, and other negligent acts and omissions of federal officers and employees in the performance of contractual and statutory duties. Moreover, it is also an action for unfair and deceptive practices under the Tennessee Consumer Protection Act, breach of contract and breach of express and implied warranties by private contractors. This action also seeks a declaration of the responsibilities and obligations of the Farmers Home Administration under the Homeownership Program, 28 U.S.C. §§ 2201 and 2202, regulations promulgated pursuant thereto, and under the instruments and contracts entered into between the plaintiff and defendants.

Jurisdiction

2. This court has jurisdiction to adjudicate the causes of action enumerated in this complaint pursuant to 28 U.S.C. §§ 1331, 1346(a)(2), 1346(b), and 1361, 2201 and 2202. Furthermore, this court has pendant party jurisdiction to adjudicate the causes of action enumerated in this complaint in

that they arise out of the same transaction giving rise to jurisdiction pursuant to federal law as set forth above.

Parties

3. Plaintiff Onilea Neal is a resident and citizen of Roane County, Tennessee.

4. Defendant Robert Bergland is the United States Secretary of Agriculture, and is sued in that capacity. Defendant Bergland has over-all administrative authority and responsibility for the operations of the Farmers Home Administration (hereinafter referred to as "FmHA") and its employees, and is charged with the duty to ensure that the FmHA and its employees perform their functions and meet FmHA's loan contract obligations in conformity with all statutes and regulations applicable thereto.

5. Defendant Gordon Cavanaugh is the National Administrator of Farmers Home Administration, and is sued in that capacity. As National Administrator, defendant Cavanaugh is charged by 7 U.S.C. § 1981 with the duty of administering and supervising the operations and activities of the FmHA in conformity with all laws and regulations applicable thereto, and with the obligation to faithfully fulfill the statutory objectives and contractual obligations of FmHA.

6. Defendant Earl Wayne Avery is the State Director for the State of Tennessee and is sued individually and in that capacity. As State Director, defendant Avery has direct responsibility for the supervision of the employees of FmHA within the State, and is charged with the obligation to ensure that the actions taken by FmHA employees comply with all applicable laws and regulations, and that the objectives and contractual obligations of FmHA are fulfilled.

7. Defendants S. Lain Parkison and Mary C. Wells are the FmHA Supervisor and Assistant Supervisor, respectively, for the County of Roane, Tennessee, and are sued individually and in their respective capacities. As County Supervisor and Assistant County Supervisor, defendants S. Lain Parkison and Mary C. Wells are charged with the re-

sponsibility for receiving, evaluating, and approving applications for FmHA assistance, ensuring that building plans, specifications, and contracts for construction financed by FmHA loans conform to FmHA standards, ensuring that actual construction under FmHA financed contracts adheres to approved plans and specifications, safeguarding the interests of both the borrower and the government, inspecting construction, and disbursing funds to pay for acceptable work which conforms to the terms of FmHA contracts.

8. Defendants C.E. Scott, Jr., Gary Humphreys and Wayne Humphreys (hereinafter referred to as "Contractors") are individuals employed by or doing business as Home Marketing Associates, Inc. Acting as employees of or doing business as Home Marketing Associates, Inc., defendant Contractors were engaged in the business of prefabricated home construction, and contracted with plaintiff for the construction of the dwelling at issue herein pursuant to a contract financed by FmHA and subject to the regulations, approval and supervision of FmHA. At all times relevant herein, defendants C. E. Scott, Jr., Gary and Wayne Humphreys were personally involved in the transaction hereinafter set forth.

9. Defendant Home Marketing Associates, Inc. (hereinafter referred to as "Home Marketing"), is a Tennessee Corporation with its principal place of business in Kingston, Roane County, Tennessee. The agent for Home Marketing is C.E. Scott, Jr.

Statutory and Regulatory Scheme

10. Farmers Home Administration is an agency of the Department of Agriculture. Pursuant to title V of the Housing Act of 1949 as amended (42 U.S.C. § 1471 *et seq.*), the Secretary of Agriculture is authorized to "determine and prescribe the standards of adequate farm housing and other buildings," to extend financial assistance in home construction and purchase for persons of low to moderate income residing in rural areas, and to require that all new

buildings be completed in conformity with the plans and specifications required by the Secretary of Agriculture.

11. Section 501 of Title V of the Housing Act of 1949 is the Homeownership Program under which borrowers may purchase, construct, repair or rehabilitate single family homes. Applicants for Section 502 loans apply directly to the office of the local County Supervisor, a federal official, who makes initial eligibility determinations. If a loan is approved, FmHA advances the funds to purchase or build the home and secure the debt through a deed of trust on the property.

12. Furthermore, "[b]uildings and repairs constructed with funds advanced pursuant to ... (Title V of the Housing Act of 1949) ... shall be supervised and inspected as required by the Secretary." 42 U.S.C. § 1476(a). Pursuant to the statutory mandate, the Secretary of Agriculture promulgated regulations which state in pertinent part:

> (1) *Responsibility for Inspection*: The County Supervisor, accompanied by the Borrower when practicable, will make final inspections as appropriate ...
>
> (2) *Frequency of Inspections*: The County Supervisor will inspect development work as frequently as necessary to assure that construction and land developments conform with the plans and specifications. ...

7 C.F.R. § 1804.4(9).

13. Thus, by statute and regulation, the FmHA is required to coordinate and supervise the entire transaction, including site development and building construction, until the loan is completely amortized or refinanced through a private lender. The supervision includes detailed planning with and counseling of borrowers. The primary objective of supervision is to assist borrowers in securing the objectives of the loan, one of which is to obtain decent, safe, and sanitary housing. 7 C.F.R. §§ 1804.61 *et seq.*, 1822.2 and 1822.7(a).

Statement of Facts

14. On or about August 16, 1976, plaintiff applied for a rural housing loan with FmHA, Roane County, Tennessee.

A copy of the application is attached hereto as Exhibit A. 7 C.F.R. § 1822.12. The application was approved and plaintiff was determined eligible for a FmHA Rural Housing Loan on or about June 9, 1977. A copy of the certification of approval is attached hereto as Exhibit G.

15. On or about July 6, 1977, and August 8, 1977, after consultation and counseling with defendant Parkison, plaintiff entered into construction contracts with defendant Home Marketing for the construction of a dwelling, Model 3B–1000B, financed by FmHA. A copy of the construction contracts are attached hereto as Exhibit B. Under the terms of construction contracts, construction was to conform to FmHA approved plans and specifications; no changes in plans and specifications were to be made by the contractor and borrower without written approval by FmHA; and FmHA was to inspect, examine and test all materials and workmanship and had the right to reject defective materials and workmanship or require its correction.

16. Upon information and belief, a plan for Model 3B–1000 was submitted to and approved by FmHA which plans purported to be for plaintiff's dwelling. 7 C.F.R. § 1804, Subpart A, Appendix C. The plans for Model 3B–1000 did not include any plan showing the layout of the heating and cooling system, including location and size of ducts, piping, registers, radiators, heating unit and room thermostat. Upon information and belief, the state office for the FmHA in Nashville did have plans on file for Model 3B–1000B. However, those plans were not forwarded to the office of the County Supervisor, Roane County, Tennessee. Specifications by way of "Description of Materials" was submitted in accordance with 7 C.F.R. § 180, Subpart A. Appendix C. Under paragraph 23 of the "Description of Materials," the heating system was identified as electric, "General Electric," "220 volts," "output 15 kw Btuh". The cooling equipment was identified as "central system 2 ton air conditioner 15 kw."

17. During the process of construction, three inspections were made by FmHA. The first inspection was made on

August 24, 1977, when the dwelling of the plaintiff was two percent completed. The inspection notes "Footings OK" and was signed by defendant Mary C. Wells. The second inspection was made on September 19, 1977, when the dwelling of plaintiff was ninety-nine percent completed. There were no notes or comments and the report was signed by defendant Mary C. Wells. A final inspection was made on October 3, 1977, when the dwelling of plaintiff was one hundred percent completed. No notes or comments were made in the report. The report was signed by defendant Mary C. Wells and the plaintiff.

18. In August, 1977, plaintiff, Home Marketing and FmHA closed the sale of the constructed dwelling as evidence by the Deed of Trust and Promissory Note executed by plaintiff. Copies of the Deed of Trust and Promissory Note are attached as Exhibits C and D, respectively. A one year builder's warranty was executed by Home Marketing as required by FmHA. The express warranty promises that the building is constructed in conformance with drawings and specifications approved by FmHA and Minimum Property Standards published by the Department of Housing and Urban Development. The warranty is applicable "to all workmanship, materials and the installation of equipment" including the heating system. The warranty specifically mentions the installation of a Chrysler heat pump, serial number 74152RS. A copy of builder's warranty is attached hereto as Exhibit E.

19. By letter of December 29, 1977, plaintiff notified FmHA and Home Marketing that her heat pump was not working properly. In addition, plaintiff indicated that she had never received any warranty book or instructions upon the operation of the heat pump. Plaintiff also indicated that the name plate on the heat pump unit was removed when installed.

20. In January, 1978, Home Marketing indicated that the heat pump unit installed in plaintiff's residence was manufactured by McGraw-Edison.

21. In February, 1978, defendant Parkison discovered a

tag inside the heat pump unit indicating a sizing of 10 kw and 240 volts.

22. In March, 1978, defendant Parkison, consulting with FmHA officials in Nashville, Tennessee, determined that the unit was defective or undersized, and requested Home Marketing to replace the unit.

23. On March 22, 1978, defendant Avery and other FmHA officials inspected the dwelling of plaintiff. In a letter to Home Marketing, dated March 29, 1978, defendant Avery outlined the following defects:

> 1. Wood porches instead of masonry as shown on plans.
>
> 2. Rear service door was not an exterior door as shown on plans.
>
> 3. Vertical chase between bath and bedroom not firestopped or sealed.
>
> 4. Bath rearranged contrary to plans.
>
> 5. No grade marks on floor joist or roof truss required by MPS.
>
> 6. Roof truss did not comply with approved plans or HUD criteria.
>
> 7. Dwelling not properly caulked.
>
> 8. Exterior paint was low quality and flaking.
>
> 9. Broken floor joist.
>
> 10. Poor plumbing workmanship.
>
> 11. The heating unit was observed to be a heat pump with 9.2 kw of auxiliary heater strips in nonconformance with specifications. Manufacturer of heat pump unit could not be determined.
>
> 12. No bridging as specifications required.
>
> 13. No sheetrock interior wall finish which rendered dwelling out of compliance with MPS fire resistance ratings and span requirements.

Defendant Avery further indicated that such defects and complaints by other families concerning dwellings constructed by Home Marketing were "of great concern to this agency." Defendant Avery instructed defendant Parkison and his supervisor to "follow up on all construction com-

plaints." A copy of the March 24, 1978 letter is attached hereto as Exhibit F.

24. On or about May 3, 1978, Home Marketing agreed with defendant Parkison and plaintiff that the heat system installed in plaintiff's home would "be changed out with one showing 15 kw heat" within 30 days.

25. On July 31, 1978, defendant Parkison requested that Home Marketing be suspended or debarred from further participation in the FmHA Rural Housing Program in part due to failure to change out the heating unit in plaintiff's dwelling.

26. In September, 1978, Home Marketing modified the heat unit in plaintiff's dwelling by adding additional auxiliary heat strips to increase the rating of the unit to 19 kw auxiliary heat capacity. No further modifications were made. Plaintiff did not receive any warranty booklet or operating instructions.

27. The heating unit in plaintiff's dwelling still does not operate properly, efficiently or safely. Plaintiff has been unable to use the heat pump unit and has had to rely upon portable electric register heaters. The Contractors have failed or refused to replace or repair the various construction defects, including but not limited to the heating and cooling system, despite requests and demands by plaintiff and representatives of FmHA.

28. On or about November 19, 1978, plaintiff requested compensation from FmHA to correct or replace her heating system and to correct other construction defects. The Administrator of FmHA has not made a final determination upon plaintiff's claim.

29. On June 6, 1979, plaintiff filed a claim against the FmHA, Department of Agriculture pursuant to 28 U.S.C. §§ 2671–2680. The Secretary of the Department of Agriculture has failed to act upon plaintiff's claim within six months from date of filing.

FIRST CAUSE OF ACTION

Breach of Contract by FmHA Defendants

30. Under applicable statutes and regulations, and by the terms of the loan commitment (Exhibit G), promissory notes (Exhibit D), and deed of trust (Exhibit C), FmHA and its employees and agents promised to provide plaintiff technical assistance including inspection and supervision of the construction of plaintiff's new home and to insure that the provisions of the contract were fulfilled. FmHA and its employees further promised and owed plaintiff the duty to refuse to approve the release of funds to the builder for payment for work performed unless the work conformed to plans and specifications, or approved alterations pursuant to which the house was constructed. In relevant part, the regulations incorporated into contracts between plaintiff and FmHA provide that:

> [T]he County Supervisor must make it clear to the borrower and the payee [contractor, material man, etc.], if possible, that the checks will be countersigned *only if the quality and quantity of items purchased are in accordance with approved plans.* [Emphasis added]

7 C.F.R. § 1803.7(d)(3)(i).

> Upon completion of the whole contract and acceptance of the work by the borrower *and the County Supervisor*, and compliance by the contractor with all the items and conditions of the contract, the amount due will be paid. [Emphasis added]

7 C.F.R. § 1804.4(d)(7)(vii)(a).

31. In consideration for such promises, plaintiff executed a promissory note (Exhibit D) in favor of FmHA and is obligated to make monthly payments in the amount of $153.00.

32. During the course of construction of plaintiff's house, the contractors and Home Marketing made numerous material and substantial alterations and substitutions of building plans, materials, and equipment, such that the house as constructed differs materially and substantially from that contemplated by plaintiff and required by the construction contract. By failing to approve such alternative and substi-

tutions and by failing to render to plaintiff technical assistance, including adequate inspection and supervision of the construction of plaintiff's home, FmHA and its employees have breached its contractual obligation and duties while exacting payments from plaintiff resulting in the improper retention of said payments and damages in the amount of $10,000.

SECOND CAUSE OF ACTION

Negligence

33. FmHA and its employees are under a duty to plaintiff to supervise the entire transaction to see that the objectives of the loan are fully carried out, i.e., to assist families to improve their level of living by obtaining decent, safe, and sanitary housing.

34. FmHA defendants failed to exercise reasonable care in their supervision and planning the plaintiff's new home and negligently omitted to perform their supervisory and planning functions.

35. By reason of the negligence and omissions of FmHA and its employees, plaintiff has suffered actual damages in the amount of $10,000 and has suffered actual pain and anxiety in the amount of $10,000.

THIRD CAUSE OF ACTION

Detrimental Reliance

36. During the course of the entire transaction, defendants Parkison and Wells, County Supervisor and Assistant Supervisor, promised to perform their regulatory duties and further to aid and assist plaintiff in the complicated procedures and negotiations inherent in the construction of the new home.

37. Plaintiff was entitled to and did look to and rely upon defendants Parkison and Wells to supervise the planning and development stage of construction and to oversee the relationship between the contractor and the plaintiff.

38. Defendants Parkison and Wells are aware that plaintiff lacks expertise and knowledge of the sophisticated

transaction involved in newly constructed real estate. Due to this lack of expertise and knowledge, plaintiff was unable to adequately and competently inspect the construction of her new house and to monitor compliance with specifications and plans.

39. Defendants Parkison and Wells should have expected that their promises would induce action on the part of plaintiff of a substantial character, and, in fact, the promises of defendants Parkison and Wells did induce action on the part of the plaintiff by entering into a contract with defendant Home Marketing and loan payments to the FmHA.

40. As a result of such reliance on the promises of defendants Parkison and Wells, and as a result of said defendants' failure to keep such promises, plaintiff has been damaged in the amount of $10,000.

FOURTH CAUSE OF ACTION

Breach of Contract by Contractor

41. Defendant Contractors and Home Marketing made material and substantial alterations to and substitution of contractual plans and materials, such that the house as constructed differs materially and substantially from that contemplated by plaintiff and required by the construction contract.

42. By reason of the substitutions and alterations, the value of the house has been reduced and plaintiff has deem [*sic*] damaged in the amount of $10,000.

FIFTH CAUSE OF ACTION

Breach of Express Warranty

43. Defendant Contractors and Home Marketing executed a builder's warranty upon completion of plaintiff's home. This document expressly warranted that the home was in substantial conformity with minimum property standards and plans and specifications approved by FmHA. Within the time period of the warranty, plaintiff gave notice to defendant Contractors, Home Marketing, and the

FmHA that the home constructed by defendant Contractors did not conform to the agreed upon plans and specifications.

44. Plaintiff's home, as constructed by defendant Contractors and Home Marketing does not meet the standards delineated in the warranty.

45. Due to the failure of defendant Contractors and Home Marketing to conform and adhere to the terms of the warranty, plaintiff has been damages [*sic*] in the amount of $10,000.

SIXTH CAUSE OF ACTION

Breach of Implied Warranties of Workmanlike Construction and Habitability

46. Defendant Contractors and Home Marketing agreed to construct plaintiff's home and warranted that such home would meet certain minimum standards and certain plans and specifications set forth and approved by FmHA.

47. Defendant Contractors and Home Marketing held themseives out as skilled builders capable of constructing a home in a reasonable workmanlike manner.

48. Plaintiff purchased the home at issue in this case in reliance upon the skill and implied representation of Contractors and Home Marketing as to their workmanship and ability to produce a home constructed in a workmanlike manner.

49. An implied warranty arises from the contractual relationship between plaintiff and defendant Contractors and Home Marketing that the newly constructed house, built and sold by defendant Contractors and Home Marketing will be built in a workmanlike manner and suitable for habitation.

50. Defendant Contractors and Home Marketing have breached their implied warranties and rendered the plaintiff's home unhabitable and unsafe by, including but not limited to:

a. Substituting wood porches for concrete porches;

b. Failing to apply sheetrock to interior walls in order to meet minimum fire resistance ratings;

c. Failing to construct a solid perimeter foundation;

d. Improper and unsafe installation of the water heater;

e. Improper installation of drain pipe plumbing which subjects plaintiff to health hazards;

f. Failure to install floor joist hangers;

g. Substituting the heating unit required in the specifications and contract between the parties with an undersized and different heating unit;

h. Improper installation of the heating and cooling equipment, vents, duct, etc.; and

i. Rendering the operating of the heating system unsafe.

51. Defendant Contractors and Home Marketing have breached their implied warranties to build plaintiff's home in a workmanlike manner and suitable for habitation resulting in damage to plaintiff in the amount of $10,000.

SEVENTH CAUSE OF ACTION

Unfair and Deceptive Practices

52. By representing in contract and by warranty that the heating unit and system installed into plaintiff's home was of a particular make, size and capacity when in fact the heating unit and system was of a different and inferior make, size and capacity, defendant Contractors and Home Marketing have engaged in unfair or deceptive acts prohibited under the Tennessee Consumer Protection Act, T.C.A. 47–18–101 *et seq.*

53. The unfair or deceptive acts of practices of defendant Contractors are willful or knowing violations of the Tennessee Consumer Protection Act, T.C.A. 47–18–101 *et seq.*

54. As a result of the willful or knowing unfair and deceptive practices of defendant Contractors and Home Marketing, the plaintiff has suffered damages of $10,000 and is entitled to treble damages, plus costs and attorney fees.

EIGHTH CAUSE OF ACTION

Mandamus

55. Congress enacted and established a Rural Housing Insurance Fund which provides:

> The Secretary [of Agriculture] is authorized, after October 1, 1977, with respect to any unit or dwelling newly constructed during the period beginning eighteen months prior to October 12, 1977 and purchased with financial assistance by this subchapter [Title V of the Housing Act of 1949 as amended, 42 U.S.C. § 1471 *et seq.*] which he finds to have structural defects to make *expenditures* for (1) correcting such defects, (2) paying the claims of the owner of the property arising from such defects, or (3) acquiring title to the property, if such assistance is requested by the owner of the property .... *Expenditures* pursuant to this subsection may be paid from the Rural Housing Insurance Fund. [emphasis added]

42 U.S.C. § 1479(c).

56. Pursuant to 42 U.S.C. § 1479(d), the Secretary of Agriculture promulgated regulations to "prescribe the terms and conditions under which *expenditures and payments* may be made under the provisions of [42 U.S.C. § 1479(c)]." [emphasis added] These regulations are found at 7 C.F.R., Part 1924, Subpart F. A copy of these regulations are attached hereto as Exhibit H. These regulations provide, in pertinent part:

> § 1924.253 Definitions
>
> For purposes of this Subpart, the following definitions will apply:
>
> (a) Justified complaints. A complaint is justified if FmHA determines that:
>
> (1) The construction is defective in workmanship, material, or equipment, or
>
> (2) The dwelling has not been built in substantial compliance with the approved drawings and specifications, or
>
> (3) The dwelling does not comply with FmHA's Minimum Property Standards, in effect at the time the

loan was approved on the conditional commitment issued, or

(4) The property does not meet code requirements.

. . . .

(d) Structural defect. A structural defect is a defect in the dwelling or, a related facility, or a deficiency in the site or site development which directly and significantly reduces the useful life, the habitability, or the integrity of the dwelling. The defect may be due to faulty material, poor workmanship, or latent causes that existed when the dwelling was constructed. The term includes but is not limited to:

(1) Structural failures which directly and significantly affect the basic integrity of the dwelling such as in the foundation, footings, basement walls, slabs, floors, framing, walls, ceiling, or roof.

(2) Major deficiencies in the utility components of the dwelling or site such as faulty wiring, or failure of sewage disposal or water supply systems located on the property securing the loan.

(3) Serious defects in design or installation of heating systems or central air conditioning.

§ 1924.258 Purposes for which claims may be approved.

(a) Eligible purposes. A claim may be approved to:

(1) *Pay or reimburse* the owner for costs already paid to repair major structural defects, when made in accordance with plans and specifications approved by FmHA. *Payment* will be based on actual cost of the development and the borrower must provide evidence to reasonably establish the development cost. Payment may be made:

(i) To cover damages which are a direct result of the defect to permanent additions, remodeling, upgrading, etc., of the dwelling or related facilities, and

(ii) For costs approved by FmHA for professional reports by engineers, architects or others needed to determine cause of or means to repair the defect.

(2) *Reimburse* the owner for funds expended for emergency repairs. Emergency repairs are those re-

pairs necessary to preserve the integrity of the structure, to prevent damage or further damage to personal property or fixtures in the dwelling and related facilities, or to prevent or eliminate immediate health hazards. Receipts or other evidence of owner's expenditures must be provided.

. . .

(4) *Pay or reimburse* the borrower for temporary living expenses, miscellaneous expenses, storage of household goods and moving expenses incurred as a result of the defect. [emphasis added]

57. On or about November 29, 1978, Onilea Neal submitted a claim for compensation for construction defects in her home financed through the FmHA pursuant to 42 U.S.C. § 1479(c) and 7 C.F.R. § 1924.251 *et seq.*

58. By decisions dated May 3, 1979 (by Earl Wayne Avery) and September 13, 1979 and October 5, 1979 (by Wesley Harris, Hearing Officer for FmHA), the following items were determined to constitute structural defects:

(1) Floor joist hangers were not installed upon all floor joists;

(2) The horizontal drain pipe from the utility room to the drain pipe was not installed at a uniform alinement or slope of not less than ¼" per foot as required by minimum property standards (MPS) established by the Department of Housing and Urban Development;

(3) The use of ninety (90) degree bends in the main drain pipe did not meet MPS;

(4) There was no header over the access door to the crawl space in the foundation;

(5) Failure to install gypsum drywall to interior walls as called for by plans and specifications;

(6) Installation of ⅛" thickness panelling which does not meet MPS for flame spread rating;

(7) Loose and missing concrete block in the foundation resulting in the lack of a solid perimeter foundation;

(8) The water heater was located in an inaccessible and unsafe location;

(9) The heating and cooling (heat pump) system was not installed properly and a safe, adequate heating system, including equipment, ductwork, appendages, controls, etc., must be provided.

59. The Secretary of Agriculture has failed or refused to pay or otherwise compensate Onilea Neal for structural defects in her dwelling which is required under 42 U.S.C. 1479(c) and 7 C.F.R. 1924.251 *et seq*. By failing or refusing to pay or otherwise compensate Onilea Neal for structural defects, the Secretary of Agriculture has clearly departed from statutory authority and has failed to follow procedures outlined in regulations adopted to implement the compensation for construction defect program of the FmHA. The failure or refusal of the Secretary of Agriculture to pay or compensate Onilea Neal for construction defects in her dwelling is arbitrary, improper, and an abuse of discretion.

DEMAND FOR JURY

60. Plaintiff requests that this matter be tried before a jury on all issues triable to a jury.

PRAYER FOR RELIEF

Plaintiff prays the Court:

1. To declare the defendant Farmers Home Administration, its administrators, officers and employees, are under a statutory, regulatory and contractual duty to plaintiff to protect and counsel her in the purchase and construction of her dwelling, to enforce the terms and conditions of construction contract, to supervise and inspect construction in a thorough and competent manner, to approve alterations and substitutions of plans and materials provided by contract, and to refuse to disburse payments except for work which conforms to contract specifications or approved variations and which is performed in a workmanlike manner.

2. To enter judgment in favor of plaintiff and against FmHA defendants on each of the First and Third Cause of

Actions in the amount of $10,000, or in the alternative, set such amount off against principal of plaintiff's loan with FmHA.

3. To enter judgment in favor of plaintiff and against the FmHA defendants on the Second Cause of Action in the amount of $20,000.

4. To enter judgment in favor of plaintiff and against defendant Contractors on each of the Fourth, Fifth, and Sixth Cause of Actions in the amount of $10,000.

5. To enter judgment in favor of plaintiff on the Seventh Cause of Action in the amount of $40,000 plus costs and attorney's fees.

6. Compel the Secretary of Agriculture and FmHA defendants to pay or otherwise compensate plaintiff upon the Eighth Cause of Action in the amount of $15,000.

7. Such other and further relief as the Court may deem just, proper and equitable.

Respectfully submitted,

RURAL LEGAL SERVICES OF TENNESSEE, INC.

By /s/_____

LENNY L. CROCE
Attorney for Plaintiff
Post Office Box 3358
Oak Ridge, Tennessee 37830
Telephone: (615) 483-8454

EXHIBIT A

Consolidated
Mortgage Company Incorporated
P.O. Box 821 Kingston, Tennessee 37763

SALES AND CONSTRUCTION CONTRACT

Date July 6, 1977

1. CONTRACTING PARTIES:

Onilea Neal hereby agrees to purchase and Home Marketing Associates, Inc. hereby agrees to construct a house on the following described real estate, on the terms stated:

2. PROPERTY AND LOCATION:

☒ Proposed Construction; ☐ Under Construction; ☐ Existing Construction;
House No. HMA Model 3B–1000B, Street _____
Less Carport and Utility Room
City Kingston State Tennessee
Lot No. _____ Block _____
Subdivision _____
Lot Dimensions 100 × 180
☐ Outside Corporation ☐ Inside Corporation

3. PRICE AND TERMS:

The purchase or contract price is to be fully paid in cash, when and if the mortgage loan referred to below is approved and closed. If this loan is not approved for the amount applied for, this contract can be cancelled by the purchaser and the earnest money will be returned. The separate items involved in this transaction are:

Total Purchase or Contract Price is 19,000.00
($19,000.00)
This price covers: ☐ House & Lot or ☒ House only
If House Only, Price for Lot $2,000.00 Date _____
Earnest money paid to seller which is part of the purchase price and is a guarantee of performance by the purchaser, receipt

of which is hereby acknowledged _____ $_____

The Warrantor is to be Home Marketing Association, Inc.

Mortgage Loan Applied for: Conv. $_____ GI $_____

FmHA $21,170.00 TERM OF LOAN _____

Buyer is to pay Loan Cost and/or Prepaid Items which are costs in excess of the Total Purchase Price unless otherwise stated herein.

Unless otherwise stated below it is understood that the purchaser has applied for or will apply for immediately the necessary mortgage loan to conclude this contract and will furnish needed papers and information as required for the approval of this loan. Also purchaser agrees to execute mortgage papers when the loan is ready to close and the terms of this contract have been carried out, otherwise earnest money is to be forfeited and in addition thereto, the contractor may at his option sue for specific performance or for such damages as he may suffer.

4. COMPLETION IF PROPOSED CONSTRUCTION OR UNDER CONSTRUCTION:

If proposed construction or under construction, the house is to be completed substantially in conformity with plans and specifications accepted and agreed to by purchaser and seller. Also, if the dwelling is being built under FHA or VA inspection, the house is to be completed in a manner to substantially conform with the plans and specifications filed with these agencies, and shall clear their inspections. These agreements on construction are to be in accordance with the warranty contract provided for in National Housing Regulations. Otherwise, this contract is not binding on the purchaser, and earnest money will be returned.

5. COMPLETION AND DELIVERY DATE:

It is agreed that the property will be ready and tendered for delivery on or before the expiration of 3 months from the date of this contract, subject to the loan having been closed by this delivery date, money from the loan being

needed for the purchaser to pay for the property. Otherwise, delivery will be the day after closing the loan.

6. SPECIAL ASSESSMENTS:

It is understood that no special assessments or improvement bonds for such as sidewalks, curbs, gutters and sewers are now outstanding against this property and that none such off-site improvements that must be paid by the present or future owner of the property described herein are under construction or included in plans and specifications or will be commenced or completed by the time of the closing of the loan. Otherwise, such shall be paid by the seller. Furthermore, it is understood that any future special assessments that develop after the closing of the loan are to be paid by the purchaser. This paragraph would not be applicable to a builder that is agreeing to construct a dwelling on the purchaser's lot, this lot having been acquired previously and which lot is in no way connected with this sale or contract except as a lot on which the dwelling is to be built. Agreements and understanding in connection with any special assessments are as outlined above unless changed by statements made in the space below.

7. 235—AMENDMENT

We the undersigned, certify that no application fee has been or will be collected from the proposed borrower unless a firm commitment is issued on behalf of the borrower. This shall apply to persons making application under FHA Section No. 235.

8. GOOD TITLE:

In case merchantable title cannot be obtained that is acceptable to the lender or title insurance secured, earnest money is to be returned and this trade cancelled. The seller shall convey said property to the purchaser by deed free of encumbrances except taxes that are not yet payable, also restrictive covenants and easements of record, unless otherwise stated herein. This paragraph 8 is not applicable if this contract covers a house to be built on land now owned and previously acquired by the purchaser in which situation the purchaser will protect the builder from any loss oc-

curing from a defective title that cannot be insured in a way acceptable to a prudent lender.

9. EFFECT THAT WRITTEN NOTICE TO PURCHASER OF FHA/VA VALUATION HAS ON THIS CONTRACT:

Purchaser hereby states he has been given a written notice of the FHA/VA value prior to signing this contract.

☐ Yes ☐ No

It is expressly agreed that, notwithstanding any other provisions of this contract, the purchaser shall not be obligated to complete the purchase of the property described herein or to incur any penalty by forfeiture of earnest money deposits or otherwise unless the seller has delivered to the purchaser a written statement issued by the Federal Housing Commissioner or Veterans Administration setting forth the appraisal value of the property for mortgage insurance purposes of not less than $ _____ which statement the seller hereby agrees to deliver to the purchaser promptly after such appraised value statement is made available to the seller. The Purchaser shall, however, have the privilege and option of proceeding with the consummation of this contract, without regard to the amount of the appraised valuation made by the Federal Housing Commissioner or Veterans Administration.

10. The taxes are to be prorated between the seller and purchaser as of the date of closing on a prorata calendar year basis, unless otherwise stated herein:

The hazard insurance if taken over by the purchaser is to be prorated as of the date of closing.

11. ABOUT MOVING INTO THE DWELLING:
☐ Applicable ☐ Non-Applicable

In the event the purchaser desires to move into the dwelling before the loan is closed and the sale is concluded, it may be done upon the agreement of both parties concerned with the understanding that the purchaser will pay rent in advance at the rate of $_____ per month until the loan is cleared and the seller is paid for the property. It is further agreed that any unearned part of the rent is to be refunded

to the purchaser if not earned at the time the transaction for the sale and purchase of the property is closed. If it should develop that the loan cannot be closed or that the purchaser cannot otherwise pay for the property, said purchaser agrees to vacate the dwelling within 30 days paying rent in advance on a prorate basis at the rate given above.

Home Marketing Associates, Inc.

By: /s/ WAYNE HUMPHREY
Builder

/s/ Onileba Neal
Purchaser(s)

Exhibit B

CONSTRUCTION CONTRACT

USDA–FORM FHA 424–6 State Tennessee
(Rev. 2–12–71)

County Roane

This Contract, made this 8th day of August, 1977, by Onilea Neal of _____ (hereinafter called the "Owner"), and Home Marketing Associates, Inc. of Kingston, TN 37763 (hereinafter called the "Contractor").

WITNESSETH that the parties hereto agree as follows:

(A) The Contractor will furnish materials and perform the work for

The construction of a dwelling on the property of Onilea Neal

for the consideration of nineteen thousand and no/100 dollars ($19,000.00), in accordance with the "General Conditions" shown in this contract and the specifications and the drawings as follows:

(B) The Contractor will start work by August 10, 1977, and will complete the work by October 10, 1977 (See paragraph III of General Conditions).

(C) The Owner will make payments as follows: (Check X *proper payment clause and effectively xxxxx out all of the clauses not applicable.)*

☒ 2. PARTIAL PAYMENTS NOT TO EXCEED 60 PERCENT of the value of the work in place (less the aggregate of previous payments) will be made at intervals of 14 days. The value of work in place shall be as estimated by the contractor and approved by the Farmers Home Administration. Prior to receiving any partial payment, the contractor must furnish the owner with a statement showing the total amount owed to date for materials and labor procured under this contract and, if required by the owner or the Farmers Home Administration, must also submit evidence showing that previous partial payments were properly applied and that the current payment will be properly applied. Upon

completion of the whole contract and acceptance of the work as required hereunder, by the owner and the Farmers Home Administration, and compliance by the contractor with all terms and conditions of this contract, the amount due the contractor will be paid.

GENERAL CONDITIONS

1. CHANGES IN WORK.—The Owner may at any time, with the approval of the official designated by the Farmers Home Administration (hereinafter called the Representative), making changes in the drawings and specifications, within the general scope thereof. If such changes cause an increase or decrease in the amount due under this contract or in the time required for its performance, an equitable adjustment will be made, and this contract will be modified accordingly by a "Contract Change Order." No charge for any extra work or material will be allowed unless the same has been ordered on such contract change order by the Owner with the approval of the Representative, and the price therefor stated in the order.

II. INSPECTION OF WORK.—All materials and workmanship will be subject to inspection, examination, and test, by the Representative, who will have the right to reject defective material and workmanship or require its correction.

III. COMPLETION OF WORK.—If the Contractor refuses or fails to complete the work within the time specified in paragraph B of this contract, or any extension thereof, the Owner may, with the approval of the Representative, terminate the Contractor's right to proceed. In such event the Owner may take over the work and prosecute the same to completion by contract or otherwise and the Contractor will be liable for any excess cost occasioned the Owner thereby; and the Owner may take possession of and utilize in completing the work much materials and equipment as may be on the site of the work and necessary therefor. If the Owner does not terminate the right of the Contractor to proceed, the Contractor will continue the work, in which

event, actual damages for delay will be impossible to determine, and, in lieu thereof, the Contractor may be required to pay to the Owner the sum of $3.00 as liquidated damages for each calendar day of delay, and the Contractor will be liable for the amount thereof: *Provided, however,* That the right of the Contractor to proceed will not be terminated because of delays in the completion of the work due to unforeseeable causes beyond his control and without his fault or negligence.

IV. RELEASES.—Prior to final payment, the Contractor will submit evidence that all payrolls, material bills, and other indebtedness connected with the work have been paid as required by the Owner or the Representative.

V. OBLIGATION TO DISCHARGE LIENS.—Acceptance by the Owner and the Representative of the completed work performed by the Contractor and payment therefor by the Owner will not relieve the Contractor of his obligation to the Owner (which obligation is hereby acknowledged) to discharge any and all liens for the benefit of subcontractors, laborers, materialmen, or any other persons performing labor upon the work or furnishing material or machinery for the work covered by this contract, which have attached to or may subsequently attach to the property, or interest of the Owner.

VI. NOTICES AND APPROVAL IN WRITING.—Any notice, consent, or other act to be given or done hereunder will be valid only if in writing.

VII. EQUAL OPPORTUNITY.—The Contractor, in the performance of this contract, will comply with all applicable equal opportunity requirements.

VIII. CLEANING UP.—The contractor shall keep the premises free from accumulation of waste material and rubbish and at the completion of the work he shall remove from the premises all rubbish, implements and surplus materials and leave the building broom-clean.

IX. BUILDERS WARRANTY.—Upon completion of the work the contractor will execute Form FHA 424–19, "Builders Warranty" for new construction and rehabilitation.

(D) During the performance of this contract, the contractor agrees as follows:

(1) The contractor will not discriminate against any employee or applicant for employment because of race, color, religion, sex or national origin. The contractor will take affirmative action to ensure that applicants are employed, and that employees are treated during employment, without regard to their race, color, religion, sex or national origin. Such action shall include, but not be limited, to the following: employment, upgrading, demotion or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The contractor agrees to post in conspicuous places, available to employees and applicants for employment, notices to be provided by the Farmers Home Administration setting forth the provisions of this nondiscrimination clause.

(2) The contractor will, in all solicitations or advertisements for employees placed by or on behalf of the contractor, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex or national origin.

(3) The contractor will send to each labor union or representative of workers with which he has a collective bargaining agreement or other contract or understanding, a notice, to be provided by the Farmers Home Administration, advising the said labor union or workers' representative of the contractor's commitments under this agreement as required pursuant to section 301 of Executive Order 11246 of September 24, 1965, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

(4) The contractor will comply with all provisions of such Executive Order and of all relevant rules, regulations, and orders of the Secretary of Labor and of any prior authority which remain in effect.

(5) The contractor will furnish all information and reports required by such Executive Order, rules, regulations, and orders, or pursuant thereto, and will permit access to his books, records, and accounts by the Farmers Home Administration and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations, and orders.

(6) In the event of the contractor's noncompliance with the nondiscrimination clauses of this contract or with any of the said rules, regulations, or orders, this contract may be cancelled, terminated or suspended in whole or in part and the contractor may be declared ineligible for further contracts in accordance with procedures authorized in such Executive Order and such other sanctions may be imposed and remedies invoked as provided in the Executive Order or by any such rules, regulations, or order, or as otherwise provided by law.

(7) The contractor will include the provisions of paragraphs (1) through (7) in every subcontract or purchase order, unless exempted by such rules, regulations, or orders, so that such provisions will be binding upon each such subcontractor or vendor. The contractor will take such action as the Farmers Home Administration may direct as a means of enforcing such provisions, including sanctions for noncompliance: *Provided, however,* that in the event the contractor becomes involved in, or is threatened with, litigation with a subcontractor or vendor as a result of such direction by the Farmers Home Administration, the contractor may request the United States to enter into such litigation to protect the interest of the United States.

The provisions of this "Equal Opportunity Clause" are not applicable to any contract not exceeding $10,000.

IN WITNESS WHEREOF, the parties hereto have executed this contract as of the date first above written.

/s/ _____

HOME MARKETING ASSOC. INC.
WAYNE HUMPHREY Sec-Treas.
Contractor

Exhibit C

REAL ESTATE DEED OF TRUST FOR TENNESSEE
Form FmHA 427 1 TN
(Rev. 9–11–75)

THIS DEED OF TRUST is made and entered into by and between the undersigned Onilea Neal, single[,] residing in Roane County, Tennessee, whose post office address is Church Street, Kingston, Tennessee 37763 as grantor(s), herein called "Borrower," and GLENN J. HAMLETT, State Director, Farmers Home Administration, Nashville, Tn[.,] as trustee, herein called "Trustee," and the United States of America, acting through the Farmers Home Administration, United States Department of Agriculture, as beneficiary, herein called the "Government," and:

WHEREAS Borrower is indebted to the Government as evidenced by one or more promissory note(s) or assumption agreement(s), herein called "note," which has been executed by Borrower, is payable to the order of the Government, authorizing acceleration of the entire indebtedness at the option of the Government upon any default by Borrower, and is described as follows:

Date of Instrument	*Principal Amount*	*Annual Rate of Interest*	*Due Date of Final Installment*
August 8, 1977	$21,170.00	8%	August 8, 2010

And the note evidences a loan to Borrower, and the Government, at any time, may assign the note and insure the payment thereof pursuant to the Consolidated Farm and Rural Development Act, or Title V of the Housing Act of 1949;

And it is the purpose and intent of this instrument that, among other things, at all times, when the note is held by the Government, or in the event the Government should assign this instrument without insurance of the note, this instrument shall secure payment of the note; but when the note is held by an insured holder, this instrument shall not secure

payment of the note or attach to the debt evidenced thereby, but as to the note and such debt shall constitute an indemnity mortgage to secure the Government against loss under its insurance contract by reason of any default by Borrower:

NOW, THEREFORE, in consideration of the loan(s) Borrower does hereby grant, bargain, sell, convey, and assign unto trust with general warranty the following described property situated in the State of Tennessee, County(ies) of Roane, and being more particularly described as follows, to-wit:

BEGINNING at an iron pin at the common corner of the Brown property and Church Street thence South 77 deg. 36 min. East 100.0 ft. to an iron pin; thence North 30 deg. 00 min. East 143.0 ft. to an iron pin; thence North 60 deg. 00 min. West 95.3 ft. to an iron pin; thence South 30 deg. 00 min. West 173.2 ft. to the point of beginning. According to a survey by W.J. Leggins on June 23, 1977.

BEING the same property conveyed to Grantor herein by deed of record in the Register's Office for Roane County, Tennessee, in Deed Book D, Series 14, Page 321.

together with all rights, interests, easements, hereditaments and appurtenances thereunto belonging, the rents, issues, and profits thereof and revenues and income therefrom, all improvements and personal property now or later attached thereto or reasonably necessary to the use thereof, including, but not limited to, ranges, refrigerators, clothes washers, clothes dryers, or carpeting purchased or financed in whole or in part with loan funds, all water, water rights, and water stock pertaining thereto, and all payments at any time owing to Borrower by virtue of any sale, lease, transfer, conveyance or condemnation of any part thereof or interest therein-all of which are herein called "the property";

TO HAVE AND TO HOLD the property unto Trustee, his successors, grantees and assigns forever in fee simple;

IN TRUST, NEVERTHELESS, (a) at all times when the note is held by the Government, or in the event the

Government should assign this instrument without insurance of the payment of the note, to secure prompt payment of the note and any renewals and extensions thereof and any agreements contained therein, including any provisions for the payment of an insurance or other charge, (b) at all times when the note is held by an insured holder, to secure performance of Borrower's agreement herein to indemnify and save harmless the Government against loss under its insurance contract by reason of any default by Borrower, and (c) in any event and at all times to secure the prompt payment of all advances and expenditures made by the Government, with interest, as hereinafter described, and the performance of every covenant and agreement of Borrower contained herein or in any supplementary agreement.

BORROWER for himself, his heirs, executors, administrators, successors and assigns WARRANTS the property unto Trustee for the benefit of the Government against all lawful claims and demands whatsoever except any liens, encumbrances, easements, reservations, or conveyances specified hereinabove, and COVENANTS AND AGREES as follows:

(1) To pay promptly when due any indebtedness to the Government hereby secured and to indemnify and save harmless the Government against any loss under its insurance of payment of the note by reason of any default by Borrower. At all times when the note is held by an insured holder, Borrower shall continue to make payments on the note to the Government, as collection agent for the holder.

(2) To pay to the Government such fees and other charges as may now or hereafter be required by regulations of the Farmer Home Administration.

(3) If required by the Government, to make additional monthly payments of 1/12 of the estimated annual taxes, assessments, insurance premiums and other charges upon the mortgaged premises.

(4) Whether or not the note is insured by the Government, the Government may at any time pay any other amounts required herein to be paid by Borrower and not

paid by him when due, as well as any costs and expenses for the preservation, protection, or enforcement of this lien, as advances for the account of Borrower. All such advances shall bear interest at the rate borne by the note which has the highest interest rate.

(5) All advances by the Government as described by this instrument, with interest, shall be immediately due and payable by Borrower to the Government without demand at the place designated in the latest note and shall be secured hereby. No such advance by the Government shall relieve Borrower from breach of his covenant to pay. Any payment made by Borrower may be applied on the note or any indebtedness to the Government secured hereby, in any order the Government determines.

(6) To use the loan evidenced by the note solely for purposes authorized by the Government.

(7) To pay when due all taxes, liens, judgments, encumbrances, and assessments lawfully attaching to or assessed against the property, including all charges and assessments in connection with water, water rights, and water stock pertaining to or reasonably necessary to the use of the real property described above, and promptly deliver to the Government without demand receipts evidencing such payments.

(8) To keep the property insured as required by and under insurance policies approved by, delivered to, and retained by the Government.

(9) To maintain improvements in good repair and make repairs required by the Government; operate the property in a good and husbandmanlike manner; comply with such farm conservation practices and farm and home management plans as the Government from time to time may prescribe; and not to abandon the property, or cause or permit waste, lessening or impairment of the security covered hereby, or, without the written consent of the Government, cut, remove, or lease any timber, gravel, oil, gas, coal or other minerals except as may he necessary for ordinary domestic purposes.

(10) To comply with all laws, ordinances, and regulations affecting the property.

(11) To pay or reimburse the Government for expenses reasonably necessary or incidental to the protection of the lien and priority hereof and to the enforcement of or the compliance with the provisions hereof and of the note and any supplementary agreement (whether before or after default), including but not limited to costs of evidence of title to and survey of the property, costs of recording this and other instruments, attorneys' fees, trustees' fees, court costs, and expenses of advertising, selling, and conveying the property.

(12) Neither the property nor any portion thereof or interest therein shall be leased, assigned, sold, transferred, or encumbered, voluntarily or otherwise, without the written consent of the Government. The Government shall have the sole and exclusive rights as beneficiary hereunder, including but not limited to the power to grant consents, partial releases, subordinations, and satisfaction, and no insured holder shall have any right, title or interest in or to the lien or any benefits hereof.

(13) At all reasonable times the Government and its agents may inspect the property to ascertain whether the covenants and agreements contained herein or in any supplementary agreement are being performed.

(14) The Government may extend and defer the maturity of and renew and reamortize the debt evidenced by the note or any indebtedness to the Government secured hereby, release from liability to the Government any party so liable thereon, release portions of the property from and subordinate the lien hereof, and waive any other rights hereunder, without affecting the lien or priority hereof or the liability to the Government of Borrower or any other party for payment of the note or indebtedness secured hereby, except as specified by the Government in writing.

(15) The power to appoint a substitute trustee is hereby granted to the Government and its assigns, to be exercised at any time hereafter, without notice and without specifying any reason therefor, by filing for record in the office

where this instrument is recorded an instrument of apointment, whereupon the substitute trustee shall succeed to all the estates, rights, powers, and trusts herein granted to or vested in Trustee, and the former trustee or substitute trustee shall be divested thereof; and notice of the exercise of this power and any requirement of, or right to require, a bond from any trustee hereunder, are hereby waived.

(16) If at any time it shall appear to the Government that Borrower may be able to obtain a loan from a production credit association, a Federal land bank, or other responsible cooperative or private credit source, at reasonable rates and terms for loans for similar purposes and periods of time, Borrower will, upon the Government's request, apply for and accept such loan in sufficient amount to pay the note and any indebtedness secured hereby and to pay for any stock necessary to be purchased in a cooperative lending agency in connection with such loan.

(17) Default hereunder shall constitute default under any other real estate, or under any personal property or other, security instrument held or insured by the Government and executed or assumed by Borrower, and default under any such other security instrument shall constitute default hereunder.

(18) SHOULD DEFAULT occur in the performance or discharge of any obligation in this instrument or secured by this instrument, or should any one of the parties named as Borrower die or be declared an incompetent, a bankrupt, or an insolvent, or make an assignment for the benefit of creditors, the Government, at its option, with or without notice, may: (a) declare the entire amount upaid under the note and any indebtedness to the Government hereby secured immediately due and payable, (b) for the account of Borrower incur and pay reasonable expenses for repair or maintenance of and take possession of, operate or rent the property, (c) upon application by it and production of this instrument, without other evidence and without notice of hearing of said application, have a receiver appointed for the property, with the usual powers of receivers in like

cases, and (d) authorize and request Trustee to foreclose this instrument and sell the property as prescribed by law or herein.

(19) Trustee may foreclose this deed of trust by advertisement and sale to the highest bidder: PROVIDED, HOWEVER, that in any deed or deeds executed by Trustee hereunder, any and all statements of fact and other recitals therein made as to the nonpayment of the money secured, the nonperformance of covenants herein, the request to Trustee to enforce this trust, the proper and due appointment of any substitute Trustee, the advertisement of sale, due publication of sale, due authorization by Trustee of his delegate to conduct the sale, or any other preliminary act or thing having been duly done by said Trustee shall be taken by courts of law and equity as prima facie evidence that said statements or recitals of state facts, and without further questioning shall be accepted as such by Borrower.

(20) Should the property be sold by the Trustee as aforesaid: (a) personal service of notice of sale need not be made, (b) the sale may be made for cash or secured credit at the option of the Government, (c) the Government and its agents may bid and purchase as a stranger, (d) borrower shall give up and deliver immediate possession of the property to the purchaser thereof or be and become a tenant unlawfully holding over and subject to summary dispossession as provided by law for such cases, (e) the Government shall be entitled to take a deficiency judgment against the borrower for any amount remaining unpaid after due application of the proceeds from said sale, and (f) Trustee at his option may conduct such sale, without being personally present, through his delegate authorized by him for such a purpose, orally or in writing.

(21) Borrower agrees that the Government will not be bound by any present or future State laws, (a) providing for valuation, appraisal, homestead or exemption of the property, (b) prohibiting maintenance of an action for a deficiency judgment or limiting the amount thereof or the time within which such actions must be brought, (c) prescribing any other statute of limitations, (d) allowing any

right of redemption or possession following any foreclosure sale, or (e) limiting the conditions which the Government may by regulation impose, including the interest rate it may charge, as a condition of approving the transfer of the property to a new borrower. Borrower expressly waives benefit of any such State laws. Borrower hereby relinquishes, waives, and conveys all rights, inchoate or consummate, of descent, dower, and curtesy.

(22) The proceeds of foreclosure sale shall be applied in the following order to the payment of: (a) costs and expenses incident to enforcing or complying with the provisions hereof, (b) any prior liens required by law or a competent court to be so paid, (c) the debt evidenced by the note and all indebtedness to the Government secured hereby, (d) inferior liens of record required by law or a competent court to be so paid, (e) at the Government's option, any other indebtedness of Borrower owing to or insured by the Government, and (f) any balance to Borrower. In case the Government is the successful bidder at foreclosure or other sale of all or any part of the property, the Government may pay its share of the purchase price by crediting such amount on any debts of Borrower owing to or insured by the Government, in the order prescribed above.

(23) All powers and agencies granted in this instrument are coupled with an interest and are irrevocable by death or otherwise; and the rights and remedies provided in this instrument are cumulative to remedies provided by law.

(24) If any part of the loan for which this instrument is given shall be used to finance the purchase, construction or repair of property to be used as an owner-occupied dwelling (herein called "the dwelling") and if Borrower intends to sell or rent the dwelling and has obtained the Government's consent to do so (a) neither Borrower nor anyone authorized to act for him will, after receipt of a bona fide offer, refuse to negotiate for the sale or rental of the dwelling or will otherwise make unavailable or deny the dwelling to anyone because of race, color, religion, sex or national origin, and (b) Borrower recognizes as illegal and hereby disclaims, and will not comply with or attempt to enforce any

restrictive covenants on the dwelling relating to race, color, religion, sex or national origin.

(25) This instrument shall be subject to the present regulations of the Farmers Home Administration, and to its future regulations not inconsistent with the express provisions hereof.

(26) Notices given hereunder shall be sent by certified mail, unless otherwise required by law, addressed, unless and until some other address is designated in a notice so given, in the case of the Government to Farmers Home Administration, United States Department of Agriculture, at Nashville, Tennessee 37203, and in the case of Borrower to him at his post office address stated above.

(27) If any provision of this instrument or application thereof to any person or circumstances is held invalid, such invalidity will not affect other provisions or applications of the instrument which can be given effect without the invalid provision or application and to that end the provisions hereof are declared to be severable.

STATE OF TENNESSEE
ROANE COUNTY

WITNESS the hand(s) and seal(s) of Borrower this 8th day of August, 1977.

The foregoing instrument and certificate were noted in Note Book L page 370 at 1:40 o'clock a.m. August 8, 1977 and Recorded in Trust Book 295 Page 222

/s/ ONILEA NEAL (SEAL)

Witness my hand.
Maggie F. Sneed /s/ _____ (SEAL)

ACKNOWLEDGMENT

By Peggy Gass Registrar

STATE OF TENNESSEE
COUNTY OF ROANE

On this 8th day of August, 1977, before me personally appeared Onilea Neal, single and _____, his wife to me known to be the person(s) described in and who executed the foregoing instrument, and acknowledged the

_____ executed the same as ____ free act and deed.

WITNESS my hand and official seal at Roane County, Kingston, Tennessee, this 8th day of August 1977.

(SEAL)

RICHARD K. EVANS
Notary Public

My commission expires: 11–21–78

Exhibit D

PROMISSORY NOTE

KIND OF LOAN
Type: Rural Housing
Pursuant to:

☐ Consolidated Farm and Rural Development Act.
☒ Title V of the Housing Act of 1949.

STATE: Tennessee
COUNTY: Roane
CASE NO.: 48–73–412–30–5265

Date August 8, 1977

FOR VALUE RECEIVED, the undersigned (whether one or more persons, herein called "Borrower") jointly and severally promise to pay to the order of the United States of America, acting through the Farmers Home Administration, United States Department of Agriculture, (herein called the "Government") at its office in Kingston, Tennessee, THE PRINCIPAL SUM OF TWENTY ONE THOUSAND, ONE HUNDRED SEVENTY AND NO/100 DOLLARS ($21,170.00), plus INTEREST on the UNPAID PRINCIPAL of EIGHT PERCENT (8%) PER ANNUM.

Payment of the said Principal and Interest shall be as agreed between the Borrower and the Government using one of four alternatives as indicated below: (check one)

☐ I. Principal and Interest Payments shall be deferred. The first installment shall be all accued interest and shall be due on _____, 19_____. Payment of Principal and later accrued Interest shall be in _____ instruments as indicated in the box below;

☒ II. Principal and Interest payments shall be deferred. The interest accrued to October 8, 1977 shall be added to the Principal. Such new Principal and later accrued Interest shall be payable in 394 regular amortized installments on the dates indicated in the box below. Borrower authorizes the Government to enter the amount of such new Principal herein $21,181.26 and the amount of such regular in-

stallments in the box below, when such amounts have been determined.

☐III. Payment of Interest shall not be deferred. Installments of accrued Interest shall be payable on the _____ of each_____ beginning on _____, 19____ through _____, 19____. Principal and later accrued Interest shall be paid in _____ installments as indicated in the box below;

____IV. Payments shall not be deferred. Principal and Interest shall be paid in _____ installments as indicated in the box below:

$153.00 on NOVEMBER 8th, 1977, and $153.00 thereafter on the 8th day of each Month until the PRINCIPAL and INTEREST are fully paid except that the FINAL INSTALLMENT of the entire indebtedness evidenced hereby, if not sooner paid, shall be due and PAYABLE THIRTY THREE (33) YEARS from the DATE of this NOTE. The consideration herefor shall support any agreement modifying the foregoing schedule of payments.

If the total amount of the loan is not advanced at the time of loan closing, the loan shall be advanced to the Borrower as requested by Borrower and approved by the Government. Approval of the Government is mandatory provided the advance is requested for a purpose authorized by the Government. Interest shall accrue on the amount of each advance from its actual date as shown on the reverse hereof. Borrower authorizes the Government to enter the amount and date of such advance in the Record of Advances.

Every payment made on any indebtedness evidenced by this note shall be applied first to interest computed to the effective date of the payment and then to principal.

Prepayments of scheduled installments, or any portion therof, may be made at any time at the option of Borrower. Refunds and extra payments, as defined in the regulations (7 C.F.R. 1861.2) of the Farmers Home Administration according to the source of funds involved, shall, after payment of interest, be applied to the installments last to be-

come due under this note and shall not affect the obligation of Borrower to pay the remaining installments as scheduled herein.

Borrower agrees that the Government at any time may assign this note and insure the payment thereof, and in such case, though the note is not held by the Government, Borrower shall continue to pay to the Government, as collection agent for the holder, all installments of principal and interest as scheduled herein.

If this note is held by an insured lender, prepayments made by Borrower may, at the option of the Government, be remitted by the Government to the holder promptly or, except for final payment, be retained by the Government and remitted to the holder on either a calendar quarter basis or an annual installment due date basis. The effective date of any prepayment retained and remitted by the Government to the holder on an annual installment due date basis shall be the date of the prepayment by Borrower, and the Government will pay the interest to which the holder is entitled accruing between the effective date of any such prepayment and the date of the Treasury check to the holder.

Borrower hereby certifies that he is unable to obtain sufficient credit elsewhere to finance his actual needs at reasonable rates and terms, taking into consideration prevailing private and cooperative rates and terms in or near his community for loans for similar purposes and periods of time, and that the loan evidenced hereby shall be used solely for purposes authorized by the Government.

Property constructed, improved, purchased, or refinanced in whole or in part with the loan evidenced hereby shall not be leased, assigned, sold, transferred, or encumbered, voluntarily or otherwise, without the written consent of the Government. Unless the Government consents otherwise in writing, Borrower (a) will personally operate such property as a farm with his own and his family's labor if this is an FO loan, or (b) will personally occupy and use such property if this is an RH loan on a "nonfarm tract" or a section 504 RH loan.

REFINANCING AGREEMENT: If at any time it shall appear to the Government that Borrower may be able to obtain a loan from a responsible cooperative or private credit source at reasonable rates and terms for loans for similar purposes and periods of time, Borrower will, at the Government's request, apply for and accept a loan in sufficient amount to pay this note in full and, if the lender is a cooperative, to pay for any necessary stock. This paragraph and the preceding paragraph shall not apply to any comaker signing this note pursuant to Section 502 of the Housing Act of 1949 to compensate for deficient repayment ability of other undersigned person(s).

DEFAULT: Failure to pay when due any debt evidenced hereby or perform any covenant or agreement hereunder shall constitute default under any other instrument evidencing a debt of Borrower owing to, insured or Guaranteed by the Government or securing or otherwise relating to such a debt; and default under any such other instrument shall constitute default hereunder. UPON ANY SUCH DEFAULT, the Government at its option may declare all or any part of any such indebtedness immediately due and payable.

This Note is given as evidence of a loan to Borrower made or insured by the Government pursuant to the Consolidated Farm and Rural Development Act or Title V of the Housing Act of 1949 and for the type of loan as is indicated in the "KIND OF LOAN" block above. This Note shall be subject to the present regulations of the Farmers Home Administration and to its future regulations not inconsistent with the express provisions hereof.

Presentment, protest, and notice are hereby waived.

/s/ _____ (SEAL)
ONILEA NEAL *(Borrower)*
_____ (SEAL)
(Spouse)

124 Kirkland Ave.
Kingston, TN 37763

RECORD OF ADVANCES

AMOUNT	DATE	AMOUNT	DATE	AMOUNT	DATE
(1) $ 2,170.00	8/8/77	(8) $		(15) $	
(2) $11,500.00	9/19/77	(9) $		(16) $	
(3) $ 7,500.00	9/30/77	(10) $		(17) $	
(4) $		(11) $		(18) $	
(5) $		(12) $		(19) $	
(6) $		(13) $		(20) $	
(7) $		(14) $		(21) $	
			TOTAL	$	

FmHA 440–16 (Rev. 11–10–75)

EXHIBIT E

BUILDER'S WARRANTY

Property Location
124 Fifth Street
Kingston, TN 37763

Name(s) and Address of Purchaser(s)/Owner(s)
Ms. Onilea Neal
124 Fifth Street
Kingston, TN 37763

For good and valuable consideration, the undersigned Warrantor hereby warrants to the Purchaser(s) or Owner(s) identified above and to his (their) successors or transferees, all of whom are hereinafter referred to as Owners that:

The building including appurtenances, located on the property identified above, is constructed or improved in substantial conformity with the drawings and specifications which have been approved in writing by the Farmers Home Administration (FmHA) as well as the applicable Minimum Property Standards (MPS), published by the Department of Housing and Urban Development (HUD) as adopted by the Farmers Home Administration. This Warranty applies to all workmanship, materials, and the installation of equipment (including, but not limited to, the heating system, water heater, ranges and refrigerator).

The Owners shall give written notice to the Warrantor promptly after the discovery of any defective condition. Such written notice must be given to the Warrantor during the period of warranty. The period of warranty shall be (a) in the case of new construction or rehabilitation, one year from the date of initial occupancy of the completed or rehabilitated building or (b) in the case of improvements made to an existing building owned by the Owners prior to the improvements being made, one year from the date of the completion of the work.

It is agreed and understood that this warranty shall apply only to those defective conditions of which the Warran-

tor has been given written notice during the period of warranty.

Warrantor further agrees that he will take any necessary actions to correct such defective conditions within 30 days of receipt of written notice. If such action is not taken within 30 days, the Owners may, at their option, contract with another party for the correction of the defects. Warrantor agrees to pay any expenses incurred by the Owners to correct defects covered by this Warranty.

This warranty shall be in addition to, and in no way reduce, all other rights and privileges which such Owners may have under any other law or instrument, and shall be binding on the Warrantor notwithstanding any provision to the contrary contained in the contract of purchase or any other instrument executed by the Owners.

This warranty is executed, in part, for the purpose of inducing the Farmers Home Administration, United States Department of Agriculture, to make, insure, or guarantee a loan on the captioned property.

If this is signed by anyone other than the Warrantor, the person signing for the Warrantor represents and certifies that he is authorized to execute same by the Warrantor and by his signature the Warrantor is bound under the terms and conditions of this warranty.

IN TESTIMONY WHEREOF, the Warrantor has signed this warranty this 3rd day of October, 1977.

HOME MARKETING ASSOCIATES, INC.
By WAYNE HUMPHREY (SEAL)
Warrantor (Signature & Title)

Kingston, TN 37763
(Warrantor's Address)

WARNING

Section 1001 of Title 18, United States Code provides: "Whoever, in any matter within the jurisdiction of any department or agency of the United States knowingly and willfully ... makes any false, fictitious or fraudulent statements or representation, or makes or uses any false writing or document knowing the same to contain any false, fictitious or fraudulent statement or entry, shall be fined not more than $10,000 or imprisoned not more than five years, or both".

NOTICE TO OWNERS: ANY NOTICE HEREUNDER MUST BE DELIVERED IN WRITING TO THE WARRANTOR NO LATER THAN October 3, 1978.

Receipt of this warranty is acknowledged this 3rd day of October, 1977.

ONILEA NEAL
Owners

NOTES:

A. Contractor to complete all three forms except dates then meet with owner to agree on warranty period, sign and give to owner with the final request for payment.

Owner to meet with Warrantor to agree on warranty period and to date and sign, retain original, and forward one copy to contractor, and one to FmHA with a final request for payment.

B. This warranty shall be required in all cases involving new construction or rehabilitation of buildings including those built under contract, those built for sale without FmHA required construction inspections and those under conditional commitment procedures.

In addition to the preceding warranty, the following appliances and/or fixtures are covered by a company warranty and/or guarantee as follows:

Appliance or Equipment	Serial & Model No.	Name and Address of Company Attn:	No. Years or Mos. of Warranty
Heating System	74152RS	Chrysler Heat Pump	1 yr.
Kitchen Range	RA171070G	General Electric	1 yr.
Water Heater	H77913644	Builders Mart of America S. Carolina	
Refrigerator	MA377386	General Electric	1 yr.
Other			
Other			
Other			
Other			
Other			

We have furnished the above company warranties and/or guarantees to the buyer for his use.

WAYNE HUMPHREY FOR
HOME MARKETING, ASSOCIATES, INC.
Signed By Warrantor

October 3, 1977
Date

NOTICE TO PURCHASER(S)/OWNER(S): ANY NOTICE OF DEFECTIVE WORKMANSHIP, MATERIALS OR NONCONFORMITY MUST BE DELIVERED TO THE WARRANTOR NO LATER THAN

(Warrantor shall insert date one (1) year from initial occupancy, date of conveyance of title or date of completion, whichever is applicable.) All plastic pipe used in this job will carry a 5-year warranty from the date shown by the Warrantor above.

HOME MARKETING ASSOCIATES, INC.
Warrantor
/s/ WAYNE HUMPHREY

Receipt of this warranty is acknowledged this 3rd day of October, 1977.

ONILEA NEAL
Purchaser(s)/Owner(s)

Exhibit F

NASHVILLE, TN 37203

March 29, 1978

Home Marketing Associates, Inc.
P.O. Box 864
Kingston, TN 37763

Gentlemen:

At the request of our Acting, District Director, Mr. Gordon Millner and County Supervisor, Mr. S. Lane Parkison, we inspected the Onilea Neal dwelling on March 22, 1978. This request was in response to a complaint by Mrs. Neal. The inspection revealed the following:

1. Porches were constructed of wood in lieu of masonry as shown on plans.
2. Rear service door was not exterior door with lights as shown as F–994 as shown on plan but appeared to be an interior hollow core without glass.
3. Vertical chase between bath and bedroom was not firestopped or sealed.
4. Bath was rearranged from plan.
5. No grade marks were observed on floor joist or roof truss lumber as required by MPS.
6. Roof truss does not appear to comply with approved design submitted with plan, staples used in lieu of nails. Truss design must conform to HUD Criteria for trussed roof structure, 4950.2. The roof had a wavy appearance.
7. The unit was not properly caulked per MPS.
8. The exterior paint appeared to be of a low quality latex and was observed to be flaking off.
9. There was a broken floor joist under the front center bedroom.
10. The plumbing workmanship was observed to be poor.
11. The KVAC unit was observed to be a heat pump with 9.2 KW of auxiliary heater strips. Specifications called for General Electric 2 ton air conditioner and

15 KW of electric heat. Manufacturer of equipment could not be determined.

12. 1" × 3" bridging was not observed, as shown in specifications.
13. Specifications call for ½" sheetrock interior wall finish. Observed was approximately ⅛" plywood paneling. This results in a wall assembly that does not meet MPS fire resistance ratings and span requirements for interior wall finish.
14. The manufacturer failed to certify that the unit was manufactured per approved plans and specifications, MPS and Structural Engineering Bulletin as required per approval letters.

We also learned that there have been numerous construction complaints on your manufactured units by other families obtaining financing by this agency. Construction complaints, deviations from the plans and specifications and not furnishing proper certification are serious problems and of great concern to this agency.

In the future financing of housing units constructed by your company, it will be necessary that action be taken to improve quality control to insure compliance with approved plans and specifications. County offices should also be provided with certification that the unit was manufactured per approved plans and specifications, MPS and structural engineering bulletin.

We have instructed our County Supervisor and District Director to follow up on all construction complaints under the Builder's Warranty.

Sincerely,

EARL WAYNE AVERY
State Director

cc: County Supervisor, FmHA
Kingston, TN

District Director, FmHA
Kingston, TN

GBLasater:mrh

Exhibit G

PART VI—CERTIFICATION APPROVAL

36. I HEREBY CERTIFY that I am unable to obtain sufficient credit elsewhere to finance my actual needs at reasonable rates and terms taking into consideration prevailing private and cooperative rates and terms in or near my community for loans for similar purposes and periods of time. I agree to use, subject to and in accordance with regulations applicable to the type of assistance indicated above, and request payment of the sum specified herein. I certify that no part of said sum has been received.

WARNING: Section 1001 of Title 18, United States Code provides: "Whoever, in any matter within the jurisdiction of any department or agency of the United States knowingly and willfully falsifies, conceals or covers up . . . a material fact, or makes any false, fictitious or fraudulent statements or representations, or makes or uses any false writing or document knowing the same to contain any false, fictitious or fraudulent statement or entry, shall be fined not more than $10,000 or imprisoned not more than 5 years, or both."

/s/ ONILEA NEAL

(Signature of Applicant)

Date 5/31, 1977

37. COMMENTS AND REQUIREMENTS OF CERTIFYING OFFICIAL

1. Adequate insurance of not less than $19,500. and a 1 year paid premium receipt.

2. Executing Interest Credit Agreement at loan closing.

3. Collect $8. Credit Report fee at loan closing.

38. I HEREBY CERTIFY that all of the committee and administrative determinations and certifications re-

quired by Farmers Home Administration regulations prerequisite to providing assistance of the type indicated above have been made and that evidence thereof is in the docket, and that all requirements of pertinent regulations have been complied with. I hereby approve the above-described assistance in the amount set forth above, and by this document, subject to the availability of funds, the Government agrees to advance such amount to the applicant for the purposes of and subject to the conditions prescribed by Farmers Home Administration regulations applicable to this type of assistance.

/s/ S. LANE PARKISON

(Signature of Approving Official)

Date Approved: 6/9/77 Title: County Supervisor

39. TO THE APPLICANT: As of this date 6/9/77, this is notice that your application for the above financial assistance from the Farmers Home Administration has been approved, as indicated above, subject to availability of funds and other conditions required by the Farmers Home Administration. If you have any questions contact the County Supervisor.

INSPECTION REPORT

☒RH ☐ RRH ☐ W/S ☐RE ☐ State: Tenn

For Onilea Neal County: Roane

Address

Item of Develcpment	Percent Complete	Item of Development	Percent Complete
Dwelling	2%		

PERIODIC INSPECTION

Date & No. of Previous inspection No.

This inspection is Number

ITEMIZE AND DESCRIBE the significant conditions observed to be at variance with the approved plans and specifications and make your recommendations for correcting the deficiencies. Also make comments with respect to the progress of the work. In the case of development performed by the borrower method, carefully compare work accomplished with funds available and record any facts which indicate that actual costs are significantly at variance with planned costs. Check to see that deficiencies previously reported have been corrected.

Footings OK

(See attached sheets for additional comments)

DATE 8/24/77

signed: Mary C. Wells

FmHA Representative

FINAL INSPECTION

I CERTIFY that I have inspected the above listed items of development and that those shown as 100% complete have been completed in accordance with the Drawings and Specifications or other descriptive material. (Health Department approval has been given the water and waste disposal dated ____. Builder's Warranty is dated____.)

DATE _____ SIGNED _____

FmHA Representative

The undersigned gives approval of acceptance of the work constructed under the conditions of the contract and Builder's Warranty.

DATE _____ SIGNED _____

(Borrower)

DATE _____ SIGNED _____

SEE REVERSE FOR CHECK LIST & INSPECTION GUIDE

FmHA 424–12 (Rev. 10–30–74)

[p. 2]

GUIDE FOR INSPECTION OF CONSTRUCTION OF DWELLINGS AND BUILDINGS

Notices, Labor and Occupancy Observations.

☐ Yes ☐ No—The required posters displayed?

☐ Yes ☐ No—The facilities segregated?

☐ Yes ☐ No—Any evidence of employment discrimination?

GENERAL—Drainage conditions. Location of buildings with respect to property lines: Other buildings, water supply, sewage disposal, utilities, etc. Protection of materials on site.

EXCAVATION.—Earth bearing. Footing depths. Frost lines. Grades specified.

CONCRETE AND MASONRY.—Concrete mix or strength, forms, placing. Mortar mix. Width and depth of footings. Reinforcing steel. Stepped footings. Drain title. Concrete slabs on ground: Bed under slabs, wire mesh, slab thickness, finish. Termite protection. Foundation wall and pier alignment. Anchorage preparation. Dampproofing. Waterproofing. Exterior masonry: Lintels, wall thickness, height, parging, furring, wall vents, basement windows, termite protection. Masonry veneer: Lintels, thickness, airspace, flashing, felt, bonding, weepholes. Interior masonry wall: Thickness, lintels. All masonry walls: joists, tooling, pointing, flashing, prevention of mortar stains, cleaning. Masonry chimney and fireplaces: Flues, size of flues, height above ridge, thimble, chimney cap, smoke cap, smoke chambers, firebrick, hearth. Basementless areas: Clearance below joist, positive drainage.

CARPENTRY MATERIALS.—Species and grade of lumber, moisture content. Shims. Preservatives.

FRAMING.—Fire stopping. Framing at chimney. Columns. Posts. Anchorage and moisture protection. Girders. Floor joists, double joists. Headers and trimmers. Subflooring. Ceiling joists. Roof pitch. Roof rafters. Hip and valley rafters. Collar beams. Flat roofs. Trussed roof con-

struction. Studs, corner construction, corner bracing. Sill construction. Anchorage. Window and door openings. Plates. Wall sheathing. Roof sheathing. Termite protection.

EXTERIOR WALL FINISH.—Type of paper or felt. Lap. Fit at: Corner boards, door and window casings, drip cap, water table. Sills. Nails and nailing. Miter. Corner finish. Stucco.

ROOF COVERING.—Conditions of deck, underlay, starting course, exposure, nailing.

INSULATION.—Fastening of boards. Fill (to top of walls and even distribution in ceilings).

FLASHING AND CAULKING.—Flashing at: Exterior heads of openings, chimneys, intersections of roof and walls, valleys, hips, ridges. Caulking around openings.

PLUMBING.—Quality and materials. Workmanship. Excavation and backfill. Protection of pipes. Size of pipe. Cutting or notching. Joints and connections. Water supply lines: On solid ground below frost, shut-off valve, drain valve for entire system. Drainage system, vents and venting. Traps and cleanouts. Hangers and supports. Quality and type of fixtures. Location of fixtures. Fixtures securely installed. Domestic hot water heater and storage, equipment, safety, capacity.

HEATING.—Safety, capacity. Required tests, operating and maintenance instructions. Fuel storage. Check operation.

GAS (Liquefied Petroleum).—Approval markings on tank. Tank Location. Meter installation (hung properly). Protection of exposed pipe. Leakage under pressure (smell joints). Location of shut-off valve inside building. Proper ventilation of system.

ELECTRICAL.—Location of meter. Number of circuits. Provision for future circuits. Location of outlets and switches. Power suppliers' approval.

DRYWALL.—Joints, sanding, filling, taping.

GLAZING.—Quality of glass, putty, application.

LATHING AND PLASTERING.—Quality of lath, evenness, grounds, joints between wood and masonry, finishing.

MISCELLANEOUS METAL WORK.—Pipe rail, metal bucks, metal windows (setting, caulking and priming), painting.

MILLWORK.—Trim, cabinets, windows and doors, thresholds.

WEATHER STRIPPING.—Seal joints (tight and smooth).

FINISH FLOORS.—Dry storage, baseboard clearance, joints, nailing, finish, protection after laying.

SCREENING.—Screen cloth, tightness, fit operation, identification tags, paint splashes.

HARDWARE.—Materials, workmanship, operation, keys.

LIGHTING FIXTURES.—Type, bulb (light, clean).

PAINTING AND DECORATING.—Surface preparation, washable materials, lead content, application (suitable weather), nailheads.

BACKFILLING.—Around masonry, around trees. Finish grade 8 inches below wood.

LANDSCAPING.—Planting, seeding, finish grades.

FINAL.—Cleaning up: Masonry, crawl and pipe space, pipe chases, attic, vents in walls, floors, chimney bottoms, fireplace throat, glass, hardware and fixtures. Removal of debris. Closing of floor openings around pipes. Replacement of broken windows. Operation of doors and windows.

WATER SUPPLY

Location with respect to possible sources of contamination. Shaft. Protection from contamination. Construction. Watertight casing safe distance above slab and safe distance below ground surface. Grading at top of well to drain away in all directions. Size of concrete platform. Slope of concrete platform. Pump: Type, capacity, location, protection, pollution proof, frostproof. Capacity of pressure tank.

SEWAGE DISPOSAL

Location: Slope of grade, depth of ground water, existing and future water supply. Size and slope of house sewer to

septic tank. Capacity of tank. Distance of tank from foundation wall. Construction of tank. Location of disposal field (unobstructed and unshaded area). Construction of field. Minimum seepage area (determined by percolation test or recommendation of Soil Conservation Service and State Board of Health). Approval of State Board of Health.

Fornm FHA 124–12
(Rev. 1–23–67)

UNITED STATE DEPARTMENT OF AGRICULTURE
FARMERS HOME ADMINISTRATION

INSPECTION REPORT

State Tenn
For: Onilea Neal County Roane

Item of Development	Percent Complete	Item of Development	Percent Complete
Dwelling	99%		

PERIODIC INSPECTION

ITEMIZE AND DESCRIBE the significant conditions observed to be at variance with the approved plans and specifications and make your recommendations for correcting the deficiencies. Also make comments with respect to the progress of the work. In the case of development performed by the borrower method, carefully compare work accomplished with funds available and record any facts which indicate that actual costs are significantly at variance with planned costs. Check to see that deficiencies previously reported have been corrected.

Date 9/19/77 SIGNED MARY C. WELLS

Asst. County Supervisor

FINAL INSPECTION

I CERTIFY that I have inspected the above listed items of development and that those shown as 100% complete have

been completed in accordance with the plans and specifications or other descriptive material.

DATE _____ SIGNED _____

(County Supervisor)

DATE _____ SIGNED _____

(Borrower)

UNITED STATES DEPARTMENT OF AGRICULTURE
FARMERS HOME ADMINISTRATION

INSPECTION REPORT

☒ RH ☐ RRH ☐ W/S ☐ RE ☐ STATE Tenn

FOR: Onilea Neal COUNTY Roane

ADDRESS 124 Fifth Street, Kingston

Item of Development	Percent Complete	Item of Development	Percent Complete
Dwelling	100%		

PERIODIC INSPECTION

Date & No. of previous inspection No. _____

This inspection is Number _____

ITEMIZE AND DESCRIBE the significant conditions observed to be at variance with the approved plans and specifications and make your recommendations for correcting the deficiencies. Also make comments with respect to the progress of the work. In the case of development performed by the borrower method, carefully compare work accomplished with funds available and record any facts which indicate that actual costs are significantly at variance with planned costs. Check to see that deficiencies previously reported have been corrected.

_____

_____

_____

_____

_____

_____

_____

(See attached sheets for additional comments)

DATE _____ SIGNED _____

FmHA Representative

FINAL INSPECTION

I CERTIFY that I have inspected the above listed items of development and that those shown as 100% complete have been completed in accordance with the Drawings and Specifications or other descriptive material. (Health Department approval has been given the water and waste disposal date on Sewer. Builder's Warranty is dated 10/3/77.)

DATE 10/3/77 SIGNED MARY C. WELLS
FmHA Representative

The undersigned gives approval of the work constructed under the conditions of the contract and Builder's Warranty.

DATE 10/3/77 SIGNED Onilea Neal
(Borrower)

DATE _____ SIGNED _____

SEE REVERSE FOR CHECK LIST & INSPECTION GUIDE

PARTIAL TRANSCRIPT OF TESTIMONY AT HEARING UPON ONILEA NEAL'S REQUEST FOR COMPENSATION FOR CONSTRUCTION DEFECTS JULY 24, 1979

Testimony of Mary Wells, Assistant County Supervisor, Roane County, Tennessee

LENNY L. CROCE: I just have a few short questions. Did you do inspections during the construction of Ms. Neal's home, Mrs. Wells?

MRS. WELLS: Yes I did.

MR. CROCE: And your name is Mary Sue Wells? Is that correct?

MRS. WELLS: Yes it is.

MR. CROCE: Okay. And you made inspections, I believe, when Ms. Neal's house was 2% completed, 99% completed, and 100% completed. Is that correct?

MRS. WELLS: That's correct.

MR. CROCE: What did you do when you went out and inspected the house, the first time let's say?

MRS. WELL: Footing inspection.

MR. CROCE: And what was completed at that time?

MRS. WELLS: Just excavation and footings.

MR. CROCE: When you went out the second time what was completed?

MRS. WELLS: It was practically completed when it's 99%. Just a few little items, I don't recall what, hadn't been completed but it was basically about finished.

MR. CROCE: When you went out to the house did you have the plans with you?

MRS. WELLS: Yes I did.

MR. CROCE: And did you have the specifications with you?

MRS. WELLS: Yes I did.

MR. CROCE: Why then didn't you note in your inspections the fact that there was not a concrete porch?

MRS. WELLS: I didn't realize that that was in the specifications.

MR. CROCE: But you did have the plans with you? Is that correct?

MRS. WELLS: Yes.

MR. CROCE: You did have the specifications, is that correct?

MRS. WELLS: Yes.

MR. CROCE: Why didn't you make any notation concerning the fact that there was no drywall installed on the interior walls?

MRS. WELLS: I didn't notice that either.

MR. CROCE: You didn't know the house was supposed to have it?

MRS. WELLS: Well I guess I didn't check the specifications . . .

MR. CROCE: Did you not take the specifications with you or the plans with you?

MRS. WELLS: They were in the file.

MR. CROCE: But you didn't look at them then?

MRS. WELLS: I don't know; if I did I overlooked it.

MR. CROCE: Why didn't you make any notes concerning the rearrangement of the bathroom?

MRS. WELLS: I didn't realize it had been changed.

MR. CROCE: What about the heat pump? Did you check out whether or not it was a G.E.?

MRS. WELLS: I remember looking for a nameplate on it and I think I took something like a serial number.

MR. CROCE: Was this during your inspection before the house was closed?

MRS. WELLS: (inaudible) . . . final inspection.

MR. CROCE: Did you make sure that the warranty books and the operating booklets were there for Ms. Neal to have?

MR. CROCE: Do you want me to go on?

WESLEY HARRIS: Yes, why don't you. We're still going for (inaudible) minutes. We do have another side. I'm sorry; we have 30 more minutes.

MR. CROCE: I'll repeat my question. One of the things that you normally check is to make sure that the new owners or purchasers have booklets they're supposed to have, instructions they're supposed to have, information concerning the appliances they have in their house. Is that one of the things you normally do at a closing or when you do final inspections?

MRS. WELLS: I understand that the warranty says that the builder will provide and I usually just let the builder provide it without our overseeing that they hand it to them.

MR. CROCE: Mrs. Wells, what is your background as far as building inspection goes? Have you ever been a building inspector before?

MRS. WELLS: No.

MR. CROCE: Do you have any training in reading blueprints?

MRS. WELLS: (inaudible)

MR. CROCE: Do you have any forms or checks that you go to in inspecting houses?

MRS. WELLS: I usually try to go down the specifications and look at the blueprint and be sure everything is built according to the blueprints and specifications.

MR. CROCE: Do you know what Grade 2 lumber is?

MRS. WELLS: By the grade marks on it?

MR. CROCE: What if there's no grade marks on it? Is there any way that you can identify whether or not something is approximately Grade 2 lumber?

MRS. WELLS: (inaudible)

MR. CROCE: So you wouldn't know Grade 2 lumber if you saw it? You're probably like me, I wouldn't know it either.

MRS. WELLS: I'll admit I'm not an expert on construction.

MR. CROCE: Have you had *any* experience in construction?

MRS. WELLS: I've been an assistant county supervisor and assistant county supervisor in Clarksville almost 14 years, and I've had quite a bit of experience on the job.

MR. CROCE: Have you had any training seminars on building inspections, on mechanical duct work, electrical inspections, anything like that?

MRS. WELLS: No.

MR. CROCE: You've had no training seminars at all, is that correct?

MRS. WELLS: Not specifically on construction. We've had assistant county supervisors' training which means we've had some things about construction but not in great detail.

MR. CROCE: Do you know how to determine whether or not a drainage pipe is at the correct slant for so many feet or anything like that?

MRS. WELLS: No.

MR. HARRIS: Mr. Croce, what does your line of questioning have to do with our decision here today?

MR. CROCE: Well, I would submit that the inspectors for the Farmers Home Administration did not really realize all the changes we've noted; and if they didn't know then I don't think that the FmHA could expect Ms. Neal to know that there were changes in plans and what defects there were and what defects there weren't at the time she moved in, if Mrs. Wells didn't know who did the inspection for FmHA itself who were supposed to know what to look for in inspections of the plans and specifications. Therefore, I don't see how they can contend that Ms. Neal knowingly consented to substitution of a wooden porch for a concrete porch, or knowingly consented to the substitution of paneling for drywall when even the inspectors from the FmHA were not aware that those were called for or what they were supposed to be. I don't have any further questions.

HEWITT SAWYERS: Mrs. Wells, as far as training is

concerned, have you not attended state and district training meetings relevant to construction?

MRS. WELLS: Yes.

MR. SAWYERS: In this area, do the power cooperatives or the departments of electricity or what have you usually do your electrical inspections and sign off on those on the State or what have you?

MRS. WELLS: Yes, on electrical inspections they have to be approved, I think it's by a State inspector.

MR. SAWYERS: In looking at marginal home plans, might it have been a situation where most families have dealt very closely with their builders and know exactly what's going into a house and that you would have assumed that the person knew exactly what they were purchasing?

MRS. WELLS: Yes.

MR. SAWYERS: No further questions.

MR. CROCE: I have no further questions.

PRETRIAL DEPOSITION OF MARY C. WELLS, FmHA ASSISTANT COUNTY SUPERVISOR, FEBRUARY 22, 1980

[3] Q. Would you please state your name and address?

A. I'm Mary Wells. My home address is Post Office Box 112, Oliver Springs, Tennessee.

[4] Q. Where are you employed, Ms. Wells?

A. Farmers Home Administration, Kingston office.

Q. And, what's your position?

A. Assistant County Supervisor.

Q. How long have you been employed as the Roane County Assistant County Supervisor?

A. About seven years.

Q. What kind of employment did you have before that?

A. I was employed by Farmers Home Administration.

Q. Where?

A. In the Wartburg office.

Q. As what?

A. Uh, I was Assistant County Supervisor, Home in parentheses, prior, sometime prior to that. I'm not sure exactly when I became Assistant County Supervisor, but it was prior to July, 1972.

Q. Okay?

A. When I went to the Kingston office.

Q. When did you first start working for Farmers Home Administration?

A. September, 1965.

Q. And, what were you hired as?

A. Assistant County Supervisor, Home.

Q. Where?

[5] A. Wartburg.

Q. Wartburg. What was the significance of Home?

A. Well, I had some duties, in addition to loan making and so on, I had some duties concerning home management and so on, with people that had loans with us.

Q. What were those duties? What did they entail?

A. They were, had to do with gardening, home making, and record keeping, and management of, financial management, and such things as that.

Q. Did you counsel them on those things?

A. Yes.

Q. On how to build a garden, and how to budget themselves, and all those sort of things?

A. Yes.

Q. Do you still do that?

A. Not near as much as I did. My job description's been changed somewhat, and we used to make more home visits back then than we do now. Most of our work now is in the office. Back then we did a lot of home visits in the field.

Q. And, these were to people who were borrowers on a Farmers Home program?

A. Yes.

Q. Why was that activity engaged in?

A. Well, Morgan County, which Wartburg is located [6] in, was one of the poorest counties in the nation, and we had a lot of economic opportunity loans, and that position was set up for that particular county because of the high number of low income people and the high number of economic opportunity loans that we had, at that time.

Q. When you say economic opportunity loans, are you talking about, these are rural housing loans?

A. No. That's a different type of loan.

Q. Okay. What's—

A. (interposing) Economic opportunity loan was for, a loan for something that would increase the family's income, either agricultural or non-agricultural.

Q. But, that was administered through the Farmers Home Administration at that time?

A. Yes, it was.

Q. What other duties did you have while with the Wartburg office?

A. Loan making, and servicing loans.

Q. When you say servicing loans, what does that mean?

A. Collections, uh, working out payment agreements and so on.

Q. Did you also, if they got into trouble making payments, show them how they could budget themselves better?

[7] A. I tried to.

Q. That's part of the counseling service, sort of?

A. That's right.

Q. And, you say you took applications for loans, is that correct?

A. Yes.

Q. Is this the section five-oh-two loans?

A. Yes, that and other kinds, too.

Q. Did you do inspections?

A. I don't believe I had inspection authority, as I recall, I didn't have inspection authority until about the time I went, moved to the Kingston office. Then I was given appraisal authority, inspection authority, and loan approving authority. It may, I believe it was prior to '72, I'm sure it wasn't any later than '72.

Q. Okay. When you went to the Roane County office, did you receive any special training at that point?

A. When they gave me appraisal authority, they gave me some training in making appraisals.

Q. Okay. When did you go to Roane County?

A. July of 1972.

Q. Okay. And, that's approximately when you received this training in appraisal?

A. It was prior to that. I was trained in appraisals in the Wartburg office.

[8] Q. Okay. What did the training in appraisals consist of?

A. We had, uh, our state, state office personnel came up to our office, and we went out and visually made appraisals, saw the house, and then did the paper work necessary to make an appraisal.

Q. Okay. Did you rely upon certain factors when you make an appraisal? What do you look for when you make an appraisal?

A. Well, the size of a house, the type of construction, the quality of construction, location of the property, the size of the lot, lots of different factors. I don't, I don't guess that includes all of them.

Q. Do you look at current sales of real estate?

A. Yes. Replacement cost.

Q. Okay. Uh, when you say quality of construction, what makes the difference between a poorly constructed house and a well constructed house?

A. Well, when I speak quality, what I was referring to would be maybe a house that's well constructed, but the quality of materials might be of a lower quality than a more

expensive house would be. You know, if there's nicer fixtures and so on, and nicer interiors, and nicer trim on the outside, and things of that thing, nature, make the quality of the house better, and therefore it would be, [9] have a higher appraisal value.

Q. Can you give me an example?

A. Well, uh, a house of low quality would probably have a three piece bathroom fixtures, white and small bathroom area, and low quality paneling, and probably sheet rock walls, and the exterior will probably have very little, uh, trim and so on, like shutters and wrought iron and things that would decorate it, make it look like a better and nicer quality house.

Q. How do you tell the difference between the quality of paneling?

A. Well, it usually, the higher qualities usually have a better appearance, but it's, sometimes, kind of difficult to tell the, tell the difference. But, usually the better qualities have more shine and look more like real wood than the lower qualities.

Q. Okay. Does that, do you ever ask for any kind of manufacturer mark on the paneling to check what kind of grade it is, of any sort? Do manufacturers grade their paneling?

A. I'm sure it must be graded, but I'm not very familiar with the grades and so on of it.

Q. Okay. Have you received any other training?

A. I've received, uh, training from the district, at district meetings and from state office personnel. And, on appraisals, I've had a course at Roane State College on real estate appraising.

Q. On appraisals. Okay. What were the district [10] office training sessions, what did they consist of?

A. Well, different times there were different things. I know we had one on, uh, insulation. When insulation requirements were changed, we had a, I guess a half a day or a day training session on, uh, insulation. And, from time to time they have, maybe emphasized one thing or another,

but the whole, well, all Assistant County Supervisors, County Supervisors attend those district meetings, whenever they have them.

Q. Have you had any training specifically regarding inspections?

A. Well, we get some training in inspections in district meetings?

Q. What kind?

A. What kind of training?

Q. When you say some, I mean, what do they do?

A. I remember one meeting they showed us slides of what to look for, what construction's supposed to look like whenever it's, during different stages of it.

Q. When was this?

A. I don't recall. It's been, I would say three or four years ago probably.

Q. Was this prior to, uh, Ms. Neal's home being constructed?

A. I can't say for sure, 'cause I don't remember [11] when it was, but I would say it probably was.

Q. Okay. Did you get any specific training on how to read blueprints?

A. I don't know that I've much specific training on reading of blueprints, uh, like at district meetings, I don't recall. Of course, we've been trained by the state office when we were making, they were teaching me how to make appraisals and so on, I had some training in blueprint reading.

Q. Okay. What do you do when you go out and inspect a house, what do you normally do?

A. What, what are you talking about, new construction?

Q. Yeah, the first time you go out?

A. Make a footing inspection.

Q. Okay. What do you do when you make a footing inspection?

A. See that the footing's dug deep, and deep enough, so that the concrete can be poured adequately, for an adequate footing.

Q. So, you actually do the inspection before the concrete's poured?

A. That's right.

Q. You have to make sure that it's dug deep enough and everything else?

A. Yes.

[12] Q. When you say footing, does this sometimes mean the foundation, or—

A. Yes.

Q. A complete foundation, right?

A. That's right, yes.

Q. Do you take the plans out with you?

A. Yes.

Q. Okay, do you take the specifications out with you?

A. Yes.

Q. Do you take those out actually on the field with you, is that right?

A. We take the file which contains the plans and specifications.

Q. Okay. Is there some kind of checklist which you go through?

A. No, not on the footing.

Q. Okay. What do you do at the next inspection? I think Mr. Parkison mentioned there's three inspections, right?

A. The next inspection is the inspection before the walls are enclosed, on a stick built house.

Q. Okay?

A. And, we chec.. to see that the insulation is, uh, correct R value, and that it's properly installed so that there's no air, places where air can, like it's not cut off before it reaches the top of [13] the ceiling, and things like that. And, we're supposed to see the wiring and plumbing is sup-

posed to be roughed in at that inspection.

Q. Okay. Can you tell at that stage whether or not the house is being constructed in accordance with the plans, at that point in time, with the specifications?

A. Well, pretty much. You can tell where the size and the location of the windows, and doors and so on, if they're where they're supposed to be.

Q. You get a pretty good idea of the floor plan at that point in time, too?

A. Yes.

Q. Whether or not the walls are in the right place, and all that sort of thing?

A. That's right.

Q. Okay. Uh, now, do you require that the borrower go out with you at, on these first two inspections?

A. Not normally, if it's, if they're at work or something, it's not convenient, but they're welcome to go if they want to

Q. Uh, how long does it take to do a footing inspection?

A. I don't know. Ten minutes or so, I guess.

Q. How long does it take to do a inspection where, where the walls haven't been enclosed?

[14] A. I don't know. Ten or fifteen minutes, if there's no problems. Probably longer.

Q. You check all wiring during that period of time?

A. Well, of course, the wiring has, we check, well, we're supposed to see the wiring, but of course, the wiring has to be inspected by the state, a state inspector, before they're allowed to hook the electricity up.

Q. What about, do you inspect all the plumbing?

A. We don't inspect the wiring, we leave that to the, mostly to the inspector, state inspector.

Q. What about all the wiring?

A. Wiring. We leave that mostly to the state inspector.

Q. What about the plumbing?

A. Plumbing. We are supposed to see that the, the plumbing is supposed to be roughed in at that, during that inspection.

Q. Do you know what the MPS standards are for drain plumbing?

A. Well, its, PVC plastic is, uh, accepted, I believe, for, uh, for certain plumbing it's accepted, but it's not, I believe it's not on the inside of the house. It is used for drains.

Q. Do you know what the slope is supposed to be, how many inches per foot, or anything like that?

[15] A. No.

Q. Do they show you how to calculate that? Do you know how to determine the slope of so much, so many inches per foot?

A. Of plumbing?

Q. Uh-huh?

A. No.

Q. So, uh, you wouldn't really know whether or not plumbing was fixed at a proper slope?

A. Well, I wouldn't be an expert at it.

Q. Okay. Do you know whether or not you can use ninety degree bends in drain plumbing?

A. I wouldn't think that that would work very satisfactorily in many places.

Q. You know what I'm talking about, about ninety degree bends, right? Right angles?

A. Uh-huh.

Q. Okay. Why wouldn't it be satisfactory, Ms. Wells?

A. Well, if it was a drain, it'd probably get stopped up.

Q. Do you know what it takes to, uh, to make a house obtain a fire spread rating of two hundred?

A. No.

Q. You don't have any idea?

[16] A. I don't, now I don't know. I know that some

materials are more combustible than others, and I've been told that paneling is on the borderline of being a fire hazard, that sheet rock has a lot longer period of time to flame than, than a sheet rock wall would, I mean a paneling wall would.

Q. If I told you some paneling could, uh, reach a flame spread rating of two hundred and some cannot, would you know which paneling would and which paneling wouldn't?

A. No.

Q. Now, Ms. Wells, I'm going to hand you Exhibit Four, which has been identified as specifications for Ms. Neal's home. Have you seen those specifications before?

A. Yes, I have.

Q. Did you see them at the time that Ms. Neal's home was being constructed?

A. Yes.

Q. Were you fairly familiar with those?

A. Yes

(Off-the-record discussion.)

Q. Okay. We're back on the record. Are you familiar with the description of materials?

A. Yes, I am.

Q. Did you review those prior to going out and inspecting Ms. Neal's home?

[17] A. Not immediately prior.

Q. Not immediately prior?

A. No.

Q. Did you look at them before you went out and inspected, though?

A. I had the specifications in the file with me when I went.

Q. Well, my question is, did you familiarize yourself with the specifications before you went out and inspected?

A. No. Ordinarily, I would look at them when I get out to the site.

Q. Okay. So, you usually don't refer to the plans until you get out to the site?

A. No.

Q. And, I hand you what's been marked as Exhibit Five. Have you ever seen those plans before?

A. Yes.

Q. Were those plans in the file when you made your inspections?

A. Yes.

Q. They were?

A. (Witness indicates.)

Q. Did you look at those plans before you went out and did the inspections on Ms. Neal's home?

[18] A. I, I didn't look at them like the day I went out there. They were in the file when I was out there, but, uh, of course, when we were making the loan I saw them.

Q. But, I guess my question is, did you take any special requirement, any special time to review those plans to see, uh, to familiarize yourself with those plans and with those specifications?

A. No, I, it was just a standard plan that the Home Marketing had built several houses by. It was just, it was, I didn't see whether it was any different to any other houses. They were practically all the same.

Q. Did you, did you ever notice the difference between the plans which are marked as Exhibit Five and the fact that description of materials specify a model three B hyphen one thousand B?

A. No.

Q. Did you ever notice that those were two different numbers, numbers on the specifications and on the plans?

A. I didn't until after the, it had been brought to my attention.

Q. When was that?

A. It was about the time she filed suit.

Q. Okay. When you went out, let me hand you Exhibit Number Eight. Could you identify those for me.

A. Inspection reports.

[19] Q. Okay. What are the dates of those inspection reports?

A. August 24th, 1977, footing inspection. September the 19th, 1977, ninety-nine percent inspection. And, uh, October the 3rd, 1977, a hundred percent inspection.

Q. Did you make each, each of those inspections?

A. Yes, I did.

Q. Okay. When you went out on August 24th, 1977, what was done?

A. Footings were dug and ready for pouring.

Q. And, had there actually been any concrete poured?

A. I can't specifically remember. I don't suppose there was, but I, I've probably been out to a hundred since then, I can't remember.

Q. Do you recall whether or not any of the foundation was constructed yet, any of the blocks up, or anything like that?

A. I can't recall a thing about it.

Q. How much time did you spend?

A. I don't have any idea. Normally, ten or fifteen minutes, but I specifically don't remember that particular case, or that particular day.

Q. What about the, at the time that you went out on August 24th, 1977, did you take with you, uh, the plans and description [20] of materials?

A. Yes.

Q. Okay. Did you refer to those when you made any inspections?

A. I probably didn't on a footing inspection.

Q. Okay. What about the next inspection?

A. The ninety-nine percent inspection. The house was almost completed, it was the same as completed, just like a few little things that needed to be finished.

Q. What was the date of that?

A. September the 19th, 1977.

Q. How much time did you spend inspecting at that time?

A. I don't recall.

Q. Uh, you said it was ninety-nine percent completed, right?

A. Yes.

Q. Were you able to check the, uh, insulation in the walls?

A. No, because it was constructed in a factory, and, uh, it was practically finished before it was set on the site.

Q. Were you able to check, then, the plumbing in the walls, or wiring in the walls?

A. Nothing that was in the walls, they were already [21] enclosed.

Q. Okay. There's a checklist, uh, after the inspections, in quite detail, did you go through each one of those items? Did you refer to that?

A. I don't know.

Q. It says, Guide for Inspection of Construction of Dwellings and Buildings. Did you check and see whether or not all the concrete slabs were poured, the, uh, masonry places where there was supposed to be concrete blocks were right, or anything like that?

A. I check to see that the house was completely finished, or, and probably when I made the ninety-nine, I don't remember what they still had to do, but if there was a few odds and ends that hadn't been done, I would have filed it that day, I'm sure.

Q. Under framing, there's a, there's some place that's marked, under framing there's fire stopping. Did you check for fire stopping?

A. For fire stopping?

Q. Uh-huh?

A. No.

Q. And, you said that the walls were covered up, so you couldn't check the insulation, is that correct?

A. That's right.

Q. Did you check the plumbing?

A. Well, I saw that it was installed on the interior [22] and that, uh, looked under the floor for inspection, inspecting the insulation, and just whatever's visible is all I inspected.

Q. Did you inspect the drain, the main drain pipe?

A. I don't recall inspecting it specifically.

Q. If the main drain pipe had ninety degree angles in it, would you have noticed that?

A. I don't know.

Q. Well, you indicated before that you thought ninety degree bends in a drain pipe would be unusual and wouldn't be very satisfactory. I'm just saying, would you have noticed that if you had seen it at the time that you made your inspection?

A. I don't know. I might have. I might have noticed it and might not have.

Q. How much time did you spend on September 19, 1977?

A. I don't know.

Q. Do you keep time records?

A. No.

Q. When you go out on a job and when you come back in on a job?

A. We keep, uh, if we're, uh, claiming mileage, we put down when we leave and when we return. We may do ten things when we're on one trip, so there wouldn't be any way I could say how much—

[23] Q. (interposing) Do you know how long you took to inspect Ms. Neal's home on September 19th, 1977?

A. I don't recall.

Q. Okay. Now, uh, Ms. Wells, uh, were you aware that the plans and specifications called for concrete porches?

A. No, I wasn't.

Q. Why?

A. I, she was happy with the house, and I thought she got what she wanted, so—

Q. Was she out with you during the time you made the inspections on August 24th, 1977, September 19th, 1977?

A. I think, I wouldn't say for sure, but I think she was probably there on September the 19th, but I know she was there on the final inspection.

Q. Okay. But, you don't—

A. (interposing) On October 3rd.

Q. You don't remember whether or not she was with you on the other?

A. I'm not positive. I think, I think she was. I know she wasn't for the footing.

Q. Okay?

A. I think she probably was on the ninety-nine percent, but I know positively that she was there when we made the hundred percent inspection.

[24] Q. Okay. I understand. The question is, do not the plans and specifications call for concrete porches?

A. I believe that they do.

Q. Would you like to review those and make sure?

A. The specifications calls for four inch reinforced concrete porches.

Q. And, don't the plans, at least the plans you have, Exhibit Number Five, show that there's supposed to be a concrete porch?

A. It says four inches of reinforced concrete, porch.

Q. Did, uh, why didn't you put that down in your inspection report, that there was wood porches instead of concrete porches?

A. Well, we normally use concrete and, uh, wood porch interchangeably, depending on what the applicants wants in her house.

Q. I'm saying, don't, now Mr. Parkison testified earlier that, uh, when there's changes, we usually note those down in the file some place. Did you note this change down in the file any place?

A. No.

Q. Did you note it down on your inspection report?

A. No.

[25] Q. Did you tell Ms. Neal, did you ask Ms. Neal about wood porches instead of concrete porches?

A. I don't recall even noticing that it wasn't what the specifications called for.

Q. Okay. Did you notice that there were numerous ninety degree bends in the drain pipe, main drain pipe?

A. No, I didn't.

Q. Uh, do you know that MPS standards prohibit ninety degree bends in main drain pipes?

A. I don't know. I wasn't sure of it. I would have to look it up.

Q. But, you didn't notice that?

A. No.

Q. Did you, uh, notice the fact that there was not dry wall in the walls?

A. No.

Q. What do the specifications call for?

A. I'm sure they called for sheet rock. But, still, she, uh, said she was happy with the house, and she didn't have any complaints, so, ordinarily if it's a change from one to the other, either one is satisfactory wall covering, we normally let the applicant decide what kind they want, what kind of wall covering they want.

Q. Okay. But, the plans call for one half inch dry wall, is that correct?

[26] A. I'm sure that is, I don't see it on here, but I'm sure it was for sheet rock. I suspect it was half inch sheet rock.

Q. I believe it's item number fourteen, Ms. Wells?

A. Yes, it says, calls for sheet rock, one half inch, painted, taped and filled.

Q. Why didn't you make a notation of that?

A. Well, as I say, she was happy with the house, and I thought she got what she wanted in the house, so I didn't make any exceptions.

Q. Weren't you aware that there's a difference in fire spread rating between sheet rock and paneling?

A. I was aware that there is a difference, but, uh, paneling is acceptable. If the family wants paneling, we usually accept it.

Q. Are you saying that the paneling in Ms. Neal's home, according to you, it meets MPS fire ratings?

A. I don't know.

Q. You don't know?

A. I don't know.

Q. How would find out?

A. I don't know.

Q. Did you try to find out?

A. No.

Q. At the time that you inspected the dwelling on [27] September 19th, 1977, was the heating and cooling system and equipment installed?

A. Yes, it was.

Q. Did you check and see what make that was? On September 19, 1977?

A. No. I don't recall seeing a brand name on it.

Q. Did you check?

A. I checked to see that the heating system was in.

Q. Did you check to make sure that the right make was in?

A. No, I don't—

Q. (interposing) Did you check outside and see if the outside unit was on a concrete pad or not?

A. No. I don't recall checking that.

Q. Did you inspect the duct system above the house, in the attic?

A. No.

Q. You didn't inspect it at all?

A. No.

Q. Were you aware that the plans and specifications called for concrete sidewalks around the house?

A. No.

Q. You weren't?

A. No.

[28] Q. So, if you weren't aware of them, then you couldn't note it down, is that correct?

A. I guess.

Q. Did you, in fact, ever read this description of materials before you made an inspection of Ms. Neal's home?

A. I hurriedly read it. At the time we were, we had so many applications and such a heavy workload, that we were doing things too fast, I guess, and we overlooked them, and didn't do some of the things maybe we should have done. If we just had one or two loans, or ten loans, or something, we, we could look at everything and do everything exactly right, but at that time our workload was very, very high.

Q. I understand that, but my question is, do you recall ever reading these specifications before you did an inspection on Ms. Neal's home?

A. I don't know. I can't remember what happened that many years ago.

Q. Do you recall specifically checking these plans while you did your inspection?

A. No, not specifically, uh, it was just a typical modular house, and I didn't see anything, anything different from it than the others we'd been financing.

Q. So, when you went to check the porch and see if it was done, you didn't refer to porches of four inch reinforced concrete?

[29] A. I didn't check to see if that's what the specifica-

tions called for.

Q. And, when you looked around the house, you didn't see, you didn't check whether or not the specifications called for three foot wide concrete walks, four inches thick?

A. No.

Q. Were there concrete walks put in around Ms. Neal's home?

A. I don't know. I don't recall any.

Q. You didn't make any notations, did you?

A. No.

Q. On final inspection, uh, was there anything different between the time that you made your inspection at ninety-nine percent complete and a hundred percent complete?

A. I'm sure there was, but I don't know what the differences were. I, it may have liked something, like maybe a porch, or steps, or something like that, something small, or maybe possibly the landscaping. I don't recall what it was, but I'm sure it wasn't a hundred percent finished, or I would have filed it on the, in September.

Q. Okay. Did you again check the heating system in October of '77?

A. I checked to see that it was installed.

Q. Did you check the overheat ducts?

A. No.

[30] Q. You never did look at the duct then, huh?

A. No.

Q. Okay. Uh, did you refer to your plans again to make sure that everything was in conformance with the plans and specifications?

A. I don't recall referring to them.

Q. If you had, do you think you would have caught the fact that the porches were wood instead of concrete?

A. Probably would have.

Q. Uh-huh. Uh, if you had, would you have caught the fact that paneling was put up instead of what, dry wall?

A. I probably would have, but I probably wouldn't, probably wouldn't have done anything about it, because she got what, picked out what she wanted, picked out the paneling she wanted. And, that was acceptable wall covering, so therefore, we probably wouldn't have changed anything.

Q. Okay. At the time you made your inspection on 10/3/77 was the same time that, I believe, that the builder's warranty was executed, isn't that correct?

A. It was done the same day, I'm sure. It normally is.

Q. Did you check and see whether or not a Chrysler heat pump was actually installed?

A. No, I didn't check the model and make and so on.

[31] Q. Okay?

A. That's the builder's responsibility to provide the builder's warranty.

Q. Um-huh. I understand. I'm just saying, he said there was a Chrysler in there, did you check that there was a Chrysler unit in there?

A. No, I didn't.

Q. Uh, Ms. Wells, did you, how long did it take you to do the hundred percent inspection?

A. I don't know, fifteen to thirty minutes probably.

Q. Did you go outside the building?

A. Yes.

Q. Did you go underneath the house?

A. I looked underneath it, I didn't go under it.

Q. You actually didn't go in the door?

A. Huh-uh.

Q. Did you notice there wasn't a header over that door to the basement?

A. No.

Q. Did you notice any loose bricks or concrete blocks?

A. No.

Q. Did you know there was a broken floor joist?

A. No.

[32] Q. So, you actually didn't go underneath the house, you just looked in the door that goes into—

A. Yes.

Q. How big is that door?

A. I don't recall. I haven't seen the house, probably since October of '77 or '78, whatever year it was, '77 I guess. I don't think I've been up there since the final.

Q. Okay. So, you didn't actually walk underneath the house, you just looked under the house?

A. That's right.

Q. Where was the door located, do you recall?

A. It's on the lower side as I recall.

Q. Was it right in the middle of the foundation, or was it toward one end or the other?

A. I can't recall.

Q. Okay. Now, Ms. Wells, did you ever go, I think it's been referred to before, that, I don't think your counsel would object, that this was a prefabricated house, one that was assembled at a factory, is that correct?

A. Yes.

Q. Did you ever go to the factory and look at the house while it was being constructed?

A. No.

Q. So, there was no way that you ever got to see the [33] house before the walls were enclosed, is that correct?

A. Yes.

Q. So, there's no way you could check and see whether or not the studs were put in the right places, or whether or not insulation was put in there, is that correct?

A. That's correct.

Q. Do you go out to that factory now and look at the homes?

A. No.

Q. You don't?

A. It's my understanding we're not required to make

the second inspection on a manufactured house.

Q. Do you have regulations that say that?

A. I don't know. I don't know it's policy. I don't know whether it's in the book or not.

Q. Normally, you're required to make three inspections, is that correct?

A. Yes, a stick built house.

Q. Okay. Is, have you ever made an inspection where you found there was something wrong, and you noted it down?

A. Yes.

Q. What?

A. I found one of the modulars on another inspection, that had baseboard heat when it was supposed to have central heating [34] and air conditioning system.

Q. And, what did you do?

A. I got the, it was a conditional commitment which the builder was building to sell through Farmers Home financing, and agreed with the borrower, I mean the builder that we would agree to change it. We had to make a new appraisal. And, everybody initialed it and agreed to it, and we agreed to finance the same amount of money, with this baseboard heating?

Q. Okay. You required a change, basically, and that had to be in writing, is that correct?

A. That's right.

Q. Did you pay him before you got that changed, in writing?

A. No, the loan hadn't even been approved at that time, I don't think, on that particular house. It was a different situation than this.

Q. Was this after Ms. Neal's home was built?

A. It probably was. It was some, wasn't very, it's about that time period. I don't recall the date.

Q. Okay. So, in that case, you, you recognized that there was something not consistent with the plans?

A. That's right.

Q. Has there been any other instances?

A. Well, I don't know of anything major, a few [35] minor things.

Q. Like what?

A. Well, like, maybe they changed the arrangement of the bathroom, or put a room in a different place in the house, or something like this, or changed the kitchen from one side of the, side of a room to the other side, like where the sink and so on are, something like that.

Q. In order to catch those changes, wouldn't you have had to refer to a floor plan?

A. A blueprint.

Q. A blueprint, right, like Exhibit Number Five?

A. Something similar to that, yes.

Q. Uh-huh. Would you say that, uh, concrete, wood porches in lieu of concrete porches is a small item?

A. Yes.

Q. You would? I mean, you would recognize the difference?

A. The kind she has, it's just a, what, a four by five or something, a very small stoop. There wouldn't be much, I wouldn't think there'd be much difference in the value.

Q. Doesn't she, doesn't she have two porches? She has one on the rear and one on the front?

A. I don't know. They're just stoops, as I recall, which is four or five—

[36] Q. (interposing) When you say stoops, what do you mean?

A. It just means it's, it's just a place to walk up on to get to the front door or back door, with no cover.

Q. You mean one level?

A. Yes. No, no cover, no railing or anything around them.

Q. Would it surprise you to know that the front porch on Ms. Neal's house has a railing around it, and it takes

about seven or eight steps to get up to it?

A. I don't, I don't remember it being that way when I saw it last, it could be, but as I remember it, it was just a—

Q. There's a hand rail on the steps that go up about seven or eight steps, and there's a porch with a railing on it?

A. I didn't recall that—

Q. (interposing) Sits up about five feet off the ground?

A. Maybe it did when I inspected it, I wouldn't say. I don't know.

Q. That's not what you're referring to as a stoop, are you?

A. No, that's not what I call a stoop.

Q. A stoop's like one step?

A. The specifications call for a four by, four by five [37] or something like that, this blueprint does. Five or four concrete stoop.

Q. It says a porch, doesn't it, on the front porch?

A. No, the blueprint says stoop. Specifications just say under porch, but the blueprint says stoop.

Q. What about a change of floor covering from dry wall to paneling, is that something minor?

A. I would say it's rather minor, since either one's acceptable by Farmers Home.

Q. Apparently it's not, because Farmers Home says it's not, not the paneling in Ms. Neal's home. I refer you to a letter there written by Mr. Avery?

A. Well, it's supposed, the paneling's supposed to be certain thickness and so on to be acceptable, but we do still finance houses with paneling.

Q. Uh-huh. It has to be a certain thickness?

A. Yes.

Q. Did you notice that Ms. Neal had an extra closet in her living that doesn't show on the floor plans?

A. No, I didn't.

Q. Did you know that they rearranged her bathroom?

A. I didn't at the time I made the final inspection.

Q. But, you noticed it on other houses, right?

A. I thought her house was just the same as all the [38] other houses built by that same plan, except for a few minor changes.

Q. My question is, on other houses you've inspected, you noticed when they rearranged floor plans, haven't you?

A. In some cases.

Q. But, you didn't Ms. Neals?

A. No. I didn't see anything major.

Q. In some houses, you've noticed when they've put in a different type or different make of heating system, is that correct?

A. Well, the difference between baseboard heat and a central heating and air conditioning system, I noticed that, or at least on one occasion.

Q. I have no further questions[.]

PRETRIAL DEPOSITION OF WAYNE HUMPHREY, SECRETARY-TREASURER (OPERATIONS), HOME MARKETING ASSOCIATES, INC., FEBRUARY 7, 1980 [EXCERPTS]

[12] Q. How are the purchases of unit, via the Farmer's Home Administration, handled? What are the steps that you go through?

A. Okay. Let's clarify, first of all, that you are talking about a unit that we would build for the eventual consumer?

Q. That's correct, that's financed through Farmer's Home Administration?

A. All right. The first thing that we do, once a person has expressed interest in buying a home from us, is to take that person and physically show them exactly what we're going to be talking about, that we're going to sell them. That's step number one, we want them to see, or to kick the tires, on what they're going to be buying. And, if they are satisfied at that point in time, then the next step, of course, is to make a contract with this individual. Let me

clarify something. I'm talking about in a case of a person either buying a house that we have out there for speculation or if no such house as that [13] is available, then we will take them to a previous customer's home, the home is occupied, and show them that home. If they are satisfied, again, with what they see, then the next thing we're going to do is to give these people, if it's an existing speculative home, an option to purchase. If it is not, then we will simply make a contract with these persons to construct the home. Thereupon, we give the individual three sets of plans and specifications, if they are going to do it on a, what's called a construction loan basis, through the Farmer's Home Administration, to take to the Farmer's Home Administration to allocate their funds, so that the funds are brought in and held in an escrow account in a local bank, during the construction phase of the home. We have done some, few occasions. For the most part, we will simply find a lot that is satisfactory to the customer, either buy the lot or get an option to buy the lot, and go the route of what's called conditional commitment, through the Farmer's Home Administration, wherein we submit to them plans and specifications, and the plot plan of the property, where we propose, and a legal description of it, all of the information to the Farmer's Home Administration for them to make us an appraisal of value for this home. In other words, they're saying on a conditional basis, this home is valued at X dollars. It's conditional in the sense that they're not talking about a customer at this point. They're simply talking about the house and the property that it's sitting on, when completed.

Q. Are there any special conditions that you must meet [14] when the loan is financed with the Farmer's Home Administration?

A. Well, yes.

Q. What are those special conditions?

A. Well, compliance.

Q. Compliance with what?

A. With minimum property standards.

Q. Is that, are those minimum property standards those that were promulgated by Housing and Urban Development?

A. That is correct.

Q. Do you also, are you required to use various forms supplied by the Farmer's Home Administration?

A. Various forms for what reason?

Q. Well, like for the contract, like for warranties?

A. Yes.

Q. Like equal opportunity, I think, discrimination?

A. At the point in time that we close the loan, we are required to use their forms to give the warranty agreements. In the case of a pre-contract, in other words where the money is brought in and set aside in escrow account, we do sign a Farmer's Home contract prior to that. In the case of speculative building, we do not. We simply sign a standard sales form, give the people an option to purchase, which is on a Farmer's Home Administration from, and they process it from there.

Q. Okay. When the money is set aside by Farmer's Home [15] into a special escrow account, how do you get paid. Do you get paid all at once, or do you get paid in steps, or what?

A. Okay. Let me go back just one step. There's a couple of ways they do that. One way is that they request all the funds to be set aside in a local bank in an escrow account. The second way, and the way that we have, it seems like we've used most often, is when they do not. They simply set the funds aside in Missouri, I believe. And, when you reach a certain point of a construction phase, you call for an inspection, you simply say, look, I feel that I'm thirty percent, fifty percent complete with this project, and I would like at least that portion of my money. At which time they will then, if they agree with your progress to that point in time, they will then order that portion of the monies to come in that they will disburse to you.

Q. The only difference between the two arrangements is that the money is either held locally or held up in

Missouri, right?

A. Yes, and the difference in time it takes, usually ten days to fourteen days, for them to get that money out of Missouri. Whereas locally, they can write me a check. But, we've never been, as a matter of fact, I only know of one instance where the money was here on a local basis.

Q. Was that Ms. Neal's home?

A. Yes, it was.

Q. Okay. Let me ask you another question. What do you have to do before they will release the funds to you, and, they, [16] referring to Farmer's Home Administration?

A. If they agree with my point of completion, then they come out and make that inspection, at that point in time.

Q. Okay?

A. And, if they agree with my point of completion, they don't order the check, in other words, until then. And, simply when the check comes in, I'm past that point, at that point in time.

Q. What happens if [they] don't approve what's been done so far?

A. Well, they will approve a point of completion. They might say, in making their inspections, they might say, okay, here's something I have noticed, I want you to correct this. And, very well might deduct from your point of completion, the amount of work it would take to do that.

Q. So, if Farmer's Home Administration isn't satisfied with either the amount of work done, or the quality or manner in which the work is done, then they'll either not pay or they'll withhold a certain portion of that check, is that correct?

A. That would be my understanding, yes.

Q. Okay. Do you, in a non-Farmer's Home Administration financing situation, do you issue the same types of warranties as Farmer's Home Administration is required?

A. Yes.

Q. If the loan is financed through a local bank, do they

[17] require that they be allowed to inspect the premises before they issue checks?

A. I can't answer that question. I don't know. I've never financed a home through a local bank.

Q. What other financial institutions do you finance a home through?

A. FHA or VA.

Q. Okay. Do they inspect periodically before they issue a check?

A. Yes.

Q. Okay?

A. Now, let me clarify something here?

Q. Okay?

A. FHA doesn't have this program available that Farm Home has, where they will issue you funds as you progress. FHA simply guarantees a loan, and the Veterans Administration guarantees a loan, whereas the Farmer's Home Administration actually makes the loan.

Q. So, there's a difference there?

A. Yes.

Q. In your opinion, right?

A. Well, there is a difference in the disbursion of the funds.

Q. Farmer's Home actually disburses the funds themselves, right?

[18] A. That's right.

Q. They make the loan themselves, whereas FHA just guarantees a loan, and actually the money comes from a bank some place, right?

A. From FHA, yes, or VA.

Q. Yeah. But it comes from a bank?

A. That's right, a savings and loan.

Q. Yeah, just like a savings and loan, who participates in FHA financing, right?

A. That's right.

Q. But, let's say that on a VA financed home, you want to draw down thirty percent when you're thirty percent through with the work, can you do that?

A. No. See, that's, they don't get involved in the interim financing at all. They simply guarantee the permanent financing to the buyer, not to me.

Q. Okay?

A. And, I make my draws, when I'm building through the Federal Housing Authority or the Veterans Administration, if I'm building under their conditional commitment, I make my draws by setting up a construction loan at a local bank, and make those draws accordingly. Now, going back to that, yes, they come out and make that inspection as to what percentage—

Q. (interposing) The local bank does?

[19] A. Yes, because they're making a construction loan to me.

Q. Okay, so they want to make sure that when they pay some money, they know what they're getting for it, right?

A. Sure.

Q. And, so, when Farmer's Home Administration pays money, they want to make sure they're getting what they're paying for, right?

A. Yes.

Q. Are there any particular individuals with the Farmer's Home Administration that you deal with?

A. No. I deal with whoever is assigned.

Q. Okay. Do you deal in counties other than Roane County?

A. Oh, yes.

Q. Okay. What other counties besides Roane?

A. Rhea County, Bradley County, Morgan County, had some limited dealings with Blount County. As far as Tennessee counties, I'm sure there's others that I, I mentioned Rhea County, I believe.

Q. Uh-huh?

A. That's about the extent of it really.

Q. So, the difference between a Farmer's Home Administration loan for building a house, and VA or an FHA financed home, is that the Farmer's Home Administration really is like a savings and loan [20] institution, in that they front the money for the construction and actually pay you during the progress. They're not just the guarantors, they actually see that the work's done and have authority to release the money or not release the money?

A. That's, realizing, of course, there's two routes that you build under the Farmer's Home Administration, either by conditional commitment where they issue you no money during any phase of the construction, though they make inspections.

Q. Okay?

A. And, the other route, whereas they do it on what's called a contract basis, where they approve the person's loan in advance of the construction, rather than when the construction is completed.

Q. Okay. And, Ms. Neal was which?

A. In advance of construction.

Q. You've mentioned that Farmer's Home Administration have certain standards like the minimum property standards, are there any kind of standards, special standards, that Farmer's Home Administration imposes?

A. No. For the most part, their standards are minimum property standards. I was trying to think of some exception that they would, any exception that they would make to minimum property standards, they have, if I remember correctly, have been more stringent, than what minimum property standards would be.

Q. Okay?

[21] A. And, I was trying to think of a specific instance, and I can't. I think it's possibly in the amount of crawl space area, that the Farmer's Home Administration might possibly have required an additional six inches in a minimum location.

Q. Okay. What percentage of your business is done via Farmer's Home Administration loans?

A. At this present time, or in the past?

Q. Since you opened up in October, '76?

A. I would say that since we went into business that thirty percent, that might possibly have come under the Farmer's Home Administration program.

Q. Okay?

A. Realizing, of course, that we had quite a few multi-family units that we built there that took up our production, that was conventional finance.

Q. It's a substantial portion of your business, though?

A. It has been in the past. It is not at present.

Q. Okay. What must you submit in ways of plans and drawings and specifications to the Farmer's Home Administration?

A. Okay. We submit drawings in the sense of front elevation, floor plan, a cross section, and a foundation plan.

Q. I hand you what has been marked as Exhibits Thirteen and Twelve. Are those the plans that you submitted to Farmer's Home Administration?

[22] A. We have submitted this type of plan to the Farmer's Home Administration.

Q. Are there any other kinds of plans, or more detailed plans, that you submit to them?

A. To the Farmer's Home Administration?

Q. Right?

A. Now, this is a reduction of our large drawing, and they keep; or did at that time, when we were submitting these plans, which is now discontinued, but at that time, they kept a full scale drawing there in their office. And, they liked this particular plan because it didn't take up much space in file drawers.

Q. Is that the complete plan for that unit?

A. Yes.

Q. Are you aware that the Farmer's Home Administra-

tion requires drawings or plans for a heating and cooling system?

A. Um-huh.

Q. Is there such drawings or plans in those plans?

A. Not in these, no.

Q. Okay. Where are they?

A. We file those with our, when we registered with the state headquarters in Nashville, the duct layout.

Q. Do you have those plans here?

A. I do not.

Q. You don't have any plans providing the heating and [23] cooling system?

A. Here in this office at this moment?

Q. Um-huh?

A. No.

Q. If I told you that Nashville doesn't have any plans for heating and cooling systems for that unit, would you disagree with that?

A. Yes.

Q. But, you are aware that heating and cooling drawings and plans are required under Farmer's Home Administration regulations?

A. Yes.

Q. Okay. What do you consider Farmer's Home Administration roles to be, role to be, during the process of building a home? What's their role in the whole thing?

A. Well, if I were building it under conditional commitment, their primary step would be to okay the location, where the house was to be built. Second, they would make an evaluation of that plan that we submitted to them, at that location, and determine a reasonable value for that unit. If I was satisfied with this evaluation, I could then start construction. When the foundation was dug, I would then have a responsibility to call the Farmer's Home Administration for them to come out and make inspection of

that. And, then, they would make the final inspection of the home.

Q. How is that different from a role that, if I came into you [*sic*] office with twenty-five thousand dollars cash, and offered to buy a home, how is that different from what I would do?

A. What, you as an individual?

Q. Uh-huh?

A. You could do what you wanted to.

Q. Okay. So, if I wanted to, then instead of Farmer's Home doing the inspection, I could do the inspection, if I wanted to insure myself that was being done?

A. Sure.

Q. So, in essence, the Farmer's Home Administration would basically be acting like an individual citizen buying a home? Farmer's Home would inspect the house to make sure it's being properly constructed, and just like you would do if you were buying a home and wanted to insure that you were getting what you were paying for, is that correct?

A. Yes.

Q. So, in essence, the Farmer's Home Administration does what an individual buyer would do to protect his own interests, right?

A. Yes.

Q. So, you understood that Farmer's Home was responsible for and was supervising the construction of housing when it's financed through them, is that correct?

A. Well, let me say that we supervise the construction [25] of it.

Q. Okay?

A. They, you might say, they would police, to some extent the different construction phases of the home that is being built.

Q. And, did you understand, or do you understand that when Farmer's Home Administration provides the money

for the purchase of a house, that they have final approval for that house?

A. Yes.

Q. And, you don't get your funds without final approval from them?

A. I do not.

Q. Okay. Do you consider Farmer's Home to be party to the transactions between Home Marketing Associates and the home purchaser?

A. Yes.

Q. You consider that Farmer's Home Administration is a party to those contracts then, is that correct?

A. Well, I don't know if you would say they were a party to the contract, because I could give someone a contract to build the house, and they can use whatever source of financing that's available to them.

Q. Okay. I'm just saying when Farmer's Home Administration finances a loan?

A. Okay. Of course. As a matter of fact, they make [26] the inspections, and they jointly sign the check payable to me with the home buyer.

Q. So, you consider them to be a party to the transaction between you and the private individual whenever Farmer's Home Administration finances the loan?

A. My funds are based on their approval, for me to receive them.

Q. Have there been complaints by purchasers concerning the construction of homes that you've built?

A. Sure.

Q. How many?

A. I don't know how many. I don't think I've ever built a house that someone didn't have some complaint about it.

Q. Okay. What kind of complaints?

A. The leak in a water line, oh it's, you know, the standard, everyday complaints that any builder faces.

Q. What about the heating and cooling systems, have

there been other complaints?

A. I've had occasions where I would have to make repairs to systems, sure.

Q. How many?

A. Four or five.

Q. Have you ever changed out a system?

A. No.

PRETRIAL DEPOSITION OF S. LANE PARKISON, FmHA COUNTY SUPERVISOR, FEBRUARY 22, 1980
[EXCERPTS]

[4] Q. Mr. Parkison will you please state your name and address?

A. Lane Parkison, Post Office Box 803, Kingston, Tennessee.

Q. What's your current employment?

A. County Supervisor, Farmers Home Administration.

Q. How long have you held that position?

A. Seven years, no, I'm sorry, ten years.

Q. Have you been employed as County Supervisor of Roane County for ten years?

A. No, sir.

Q. How long have you been County Supervisor in Roane County?

[5] A. Three years.

Q. When did you begin that employment?

A. January, 1977.

Q. Prior to January of 1977, were you employed by Farmers Home Administration in some other county?

A. Yes.

Q. What county was that?

A. Rhea County.

Q. Were you the County Supervisor for Rhea County?

A. Yes.

Q. How long had you been County Supervisor for Rhea County?

A. Seven years.

Q. Okay. So, that would have been approximately in January of 1970?

A. June of 1970.

Q. And, did you, were you initially hired as a County Supervisor?

A. No, sir.

Q. What were you initially hired as?

A. An Assistant County Supervisor.

Q. How long were you an Assistant County Supervisor for Rhea County?

A. I was hired as an Assistant County Supervisor in [6] June of 19 and 66.

Q. Okay. Did you continue to work with Roane, with Rhea County Farmers Home Administration from '66 to when?

A. From '66 until '77.

Q. Mr. Parkison, you indicated that you were employed as an Assistant County Supervisor for Rhea County in June of 1966, is that correct?

A. I was employed as an Assistant County Supervisor in Roane County, serving Roane and Rhea Counties, in 1966.

Q. Okay. How long did you stay in that position?

A. From June of 1966 until June of 1970.

Q. Okay. And, in June of 1970, did you become the County Supervisor for Rhea County?

A. Yes, sir.

Q. And, you stayed as Supervisor for Rhea County until 1977, is that correct?

A. That's correct.

Q. Did you, what type of employment did you have prior to June of 1966?

A. I was employed by University of Tennessee in agricultural extension work from March of 1960 until June of 1966.

Q. What was your nature of employment as an agricultural extension worker?

A. Basically, I worked with 4-H Club members with [7] agricultural projects.

Q. Okay. Did this primarily have to do with livestock, raising livestock, stuff like that?

A. Right.

Q. What were your duties and responsibilities as an Assistant County Supervisor for Roane and Rhea County?

A. To assist in the receiving of applications, collecting data for determining eligibility of applicants, preparation of loan documents, collection of accounts, liquidation of accounts, basically whatever the County Supervisor needed assistance in.

Q. When you say accepting applications, what kind of applications are you talking about?

A. Applications for the farm loans, home loans, operating loans, water and sewer loans, sewer and water projects, uh, I think that's about, there's about thirty-five or forty different loans that we deal with.

Q. I understand. During the time that you were Assistant County Supervisor, did you inspect some construction?

A. Yes, I did.

Q. And, was this all types of construction?

A. Yes.

Q. And, these inspections were in conjunction with the loans that you made for construction of these projects, is that correct?

A. Yes, they were.

[8] Q. Did you receive any special training for the duties that you had as Assistant County Supervisor?

A. Yes.

Q. What kind of training was that?

A. We had a two-month in-service training in another county working with uh, it was on-job training.

Q. When was this?

A. This was in July and August of '66.

Q. What did the training consist of?

A. Everyday work and what to look for, what to do, how the, how it was done. In addition to this training, we've had several training sessions conducted by the state personnel.

Q. Okay. While you were an Assistant County Supervisor, what other training did you have besides the two-month on-the-job training? Do you recall?

A. I can't recall the exact training back that far ago. We had a week's training in the state office, and I can't remember the training that we had.

Q. When you became a County Supervisor, did you go through any addition training when you were, I guess, promoted from Assistant County Supervisor to the County Supervisor level?

A. Yes.

Q. What was that training?

A. This was done by the district director and state [9] office personnel in, uh, review of on-going loan activities.

Q. When did that take place?

A. It's a continuing type training that, uh, it starts at the time of promotion and continues.

Q. How often do you go to these training sessions?

A. We have, you could say we have some training about monthly, every time the district director comes to the office. As far as organized training, I, there's no set—

Q. What does the training consist of?

A. Reviewing what we've done, going out and looking at what has been done, uh, reviewing the instructions, seeing if we're complying.

Q. Well, that's pretty general. Do you go over new loan

programs and what they consist of?

A. Right.

Q. New forms that have to be filled out?

A. Yes.

Q. Do you receive any kind of technical training as far as building materials or construction techniques, or anything like that?

A. As these are, new programs are brought about, we do.

Q. What does that consist of?

A. Uh, normally they're conducted by the state architect or the state engineer, and it consists of review of what's going into effect.

[10] Q. Can you give me an example of what one of those training sessions are like?

A. Do you mean to describe what goes on in that entire—

Q. (interposing) Well, I want to know—

A. (interposing) Day's activities, or, uh, or just what?

Q. Well, does, let me ask this. Does the architect present to you, uh, and explain to you new changes in Minimum Property Standards and what those things mean?

A. Normally, yes.

Q. Okay. Does he go into detail, as far as saying the fire resistant standard for Minimum Property Standards has been changed, and the standards is X, and these are the things in the construction business that will comply with these standards?

A. We get into part of that, not into real detail with it, because normally it's a one-day training session.

Q. Would you know whether or not, if there was a, let me re-phrase it. Would your training include you learning what exact kind of materials are required in order to meet Minimum Property Standards or other specifications called for in construction of dwellings, any kind of dwelling that the Farmers Home Administration gives, loans money for?

A. Yes.

Q. Okay. So that if Minimum Property Standards required [11] a fire spread rating of three hundred, then you would know exactly what material was required in order to meet that count, fire spread?

A. I can look it up.

Q. Okay. You can look it up. But, that's the kind of training that would take place, is that correct?

A. Right.

Q. Okay. How many people do you supervise in the Roane County Farmers Home Administration office?

A. Three.

Q. And, who are those individuals?

A. Uh, Miss Mary Wells, Assistant County Supervisor. Martha Smith, County Office Assistant. Ruth Osborne, County Office Clerk.

* * *

[15] Q. Would it be accurate to say that the county office's major responsibility is for conducting farm and home ownership programs?

A. Okay, now, when you say farm and home ownership programs, that's correct.

Q. And, part of your duty is to keep abreast of technological changes in material, buildings in this area, is that correct?

A. Excuse me, I—

Q. Part of your responsibilities is to know about changes in specifications and building materials, that sort of thing, is that correct?

A. Yes.

[16] Q. And, if Ms. Wells has that kind of responsibility also, then she would have to be advised of that, is that correct?

A. That's correct.

* * *

[32] Q. Okay. How, let's say the loan is approved. How is, what are the duties and responsibilities of the Farmers Home Administration during the construction of the loan, the home, that's finally been approved?

A. We are required to make three inspections on the dwelling that's under, that's being constructed.

Q. And, that's the only responsibility during construction of the home?

A. We make the inspections, right.

Q. When are these inspections supposed to be made?

A. We make a footing inspection. We make a, an inspection when the framing is up before the sheet rock is put on. And, we make a final inspection.

Q. Okay. So, the first stage is at the foundation stage, [33] is that correct?

A. That's correct.

Q. The second stage is at the stage where everything, everything is in as far as the heating, plumbing, electrical work, but it's not covered up, is that basically it?

A. The plumbing and electrical are roughed in.

Q. Okay. And, then the final stage is when, supposedly everything is completed, is that correct?

A. That's correct.

Q. Is, how is the contractor paid during the construction?

A. The contractor is paid based on sixty percent of work in place.

Q. Okay. What does that mean?

A. All right. If the contractor, if the contract was for twenty thousand dollars, and the house was fifty percent complete, the contractor would have ten thousand dollars invested in it, we would pay him sixty percent of that ten thousand dollars, or we would pay him six thousand dollars.

Q. Okay?

A. When final inspection is made, he's paid the balance of his money.

Q. Is he paid after each inspection?

A. He can be.

[34] Q. Okay. What if the inspection indicates that he hasn't done something right?

A. Well, we can hold up payment until it's corrected.

Q. How is the contractor paid?

A. He is paid by check.

Q. And, where does the check come from?

A. Signed, uh, comes from the supervised bank account. The money is deposited in a supervised bank account. Or, it can be a Treasury check, if it's for a percentage completion. If it's in the supervised bank account, then the borrower and someone from Farmers Home sign the check. If it's a direct check, the borrower signs it.

Q. Okay. You mentioned this supervised account a couple of times now. What is that, Mr. Parkison?

A. The supervised bank account is a term that we use in handling monies, when it comes in to, for whatever type loan it is. This money is deposited in a local bank, the bank of the borrower's choosing, and it requires two signatures to withdraw the funds.

Q. The two signatures being?

A. The borrower and someone from Farmers Home.

Q. Okay. So, it's sort of like a construction escrow account, is that correct?

A. I don't know anything about construction escrow accounts.

Q. Okay. What are the duties and responsibilities of [35] the borrower while the home is being constructed?

A. The borrower is responsible for observing the work that's being done, being satisfied with it, and checking to see that things are being done according to the way they want them done.

Q. Okay. Then, do you require the borrower to go out with you when you make your inspections?

A. No. Except the final.

Q. Okay. What if the borrower and the contractor, or maybe Farmers Home Administration, want to make changes in the home after the construction has begun?

A. They're supposed to contact Farmers, excuse me, they're supposed to contact Farmers Home and do a change order.

Q. Okay. What do you mean, they're supposed to?

A. Well, if they're going to make a change, we like to know about it.

Q. Don't you tell the borrower that if they make any changes, they've got, you know, they've got to make them, you know, they've got to contact you?

A. We tell them.

Q. Do you tell the contractors that?

A. No.

Q. You do?

A. (Witness indicates)

Q. Okay. What happens if there's been a major change in [36] the construction plans, or change in the dwelling, and you go out there and find it, and you don't know about it? What do you do?

A. Normally we ask them, did you want this done, did you agree with this, and if it doesn't depreciate or decrease our security, we go on.

* * *

[42] Q. Uh, what about inspections? Do they, don't they, doesn't the contractor notify you when they want you to come out and inspect the house?

A. Uh, yes, sir.

Q. How much notice do they have to give you?

A. We like to get two or three days.

Q. Okay. You don't, do you go out there when they don't [43] ask you to go out there?

A. Yes.

Q. And, you expect to be allowed on the construction site, is that correct?

A. Yes.

Q. So, they have to allow you access to the construction site in order for you to make you [*sic*] inspections, is that correct?

A. Yes.

Q. And, if they want an inspection or to get some money, they notify you to come out and inspect?

A. Yes, sir.

Q. Okay. And, I think you've stated before that, as far as getting paid, that you have to sign any check that goes to the contractor, is that correct?

A. If it's in supervised bank account.

Q. All right. And, if the construction does not meet, uh, the standards of, you know, a contract, or something, you know, if they left something out that's really important, then you won't pay them until they make that repair, is that correct?

A. That's correct.

Q. So, you can hold up the funds, is that correct?

A. That's correct.

Q. What's the objective of the section five-oh-two home owner's loan program?

[44] A. The objective is to provide decent, safe and sanitary housing to meet the needs of rural residents.

Q. And, let me ask you this, Mr. Parkison[.] Uh, don't you think some of these things, like inspections and warranties, contribute toward that objective?

A. It's part of the, part of the loan process.

Q. Uh-huh. If the objective is to assure that people that, uh, in rural areas, to assure that they get safe, decent and sanitary housing, then part of the objective for making inspections and requiring warranties, and, you know, if there's something wrong, that you can withhold the money, and stuff like that, is to make sure that in fact those borrowers do get safe, decent and sanitary housing, is that correct?

A. That's correct.

* * *

[48] Q. Did you assist her at all in, uh, obtaining plans for a house or for the actual picking of what house was going to be constructed?

A. I showed her some plans that we had in the office. I told her if she wanted some modular home people to build her house, that she could see these different people. And, it was up to her to find them.

Q. Okay. Who were the people that you mentioned to her?

A. I gave her Monroe Modular, Home Marketing, Dixie Royal, as modular homes.

Q. Okay. Where is Monroe Modular located?

A. Madisonville.

Q. And, Home Marketing is located in Kingston, is that [49] correct?

A. That's correct.

Q. And, the other one was?

A. Dixie Royal is in Cookeville.

Q. Okay. How did you know about these modular builders?

A. They are approved modular homes by, excuse me, by Farmers Home Administration.

* * *

[55] Q. Why did you suggest a modular home to her?

A. Because she was wanting immediate housing.

Q. Why did she want immediate housing?

A. Because the house that she was living in was falling down.

[56] Q. Did you see the house she was living in?

A. I certainly did.

Q. Was it falling down?

A. She had a, something propping up the kitchen ceiling.

* * *

[57] Q. In addition to plans that were submitted concerning the home to be built for Ms. Neal by Home Marketing, what other documents were submitted?

A. A set of specifications.

Q. Is that what's been marked as Exhibit Four?

A. That's correct.

Q. And, that's a document entitled Description of Materials?

A. That's right.

Q. Is that a form provided by Farmers Home Administration?

A. Uh, this form is used by Farmers Home, the VA, and also HUD.

Q. Okay. What's the, uh, the model of the home that's listed there on that document?

A. Three B one thousand B.

Q. B, one thousand B?

A. That's correct.

Q. Do you have a copy of the plans of that home?

A. I do not.

Q. Okay. In other words, there's a different number [58] there than is on Exhibit Number Five, is that correct?

A. That's correct.

Q. What other documents are submitted, uh, let me back up. Who fills out the Description of Materials?

A. The applicant and the contractor.

Q. Okay. And, they're required to fill out that, to supply that information on a form which Farmers Home Administration supplies?

A. That's correct.

Q. What other documents are required, besides the plans and the description of materials?

A. Those are all that we actually require.

Q. Okay. What else was submitted, uh, in connection with Onilea Neal's home?

A. A work, worksheet for manual J on heating and cooling.

Q. Okay. Is this Exhibit Number Six?

A. That's correct.

Q. And, so that was basically part of the contract, or part of the specifications for the construction of Ms. Neal's home, is that correct?

A. That's correct.

Q. Okay. Uh, what's the date of that form, worksheet for manual J?

[59] A. 7/20/76.

Q. 26, '76?

A. '76.

Q. So, that was about a year before the contract, is that correct?

A. That's correct.

Q. Uh, is there a house model number on that?

A. I don't see one.

Q. Who's the form filled out for, what's the company it's filled out for?

A. Uh, International Unitized Housing, Incorporated.

Q. Have you had any dealings with that company?

A. Not per se.

Q. Do you know what that company is?

A. It's a different name for Home Marketing.

Q. Who told you that?

A. It's on a construction engineering bulletin issued by HUD.

Q. Do you have that with you?

A. No, I don't.

Q. Who has it?

A. There's a, the HUD office would have them, and—

Q. (interposing) HUD?

A. Um-huh.

[60] Q. Here in Knoxville?

A. I would assume they would, uh, the sheet on that.

Q. It's your understanding, then, that Home Marketing Associates and International Unitized Housing, Inc., are the same company?

A. For, they were operating out of the same place.

Q. Did you know this as of, uh, July of 1977?

A. I knew the same people were in both.

Q. When you say the same people, who do you refer to?

A. The owners of the businesses.

Q. What are their names?

A. Uh, Wayne Humphrey was the one that was representing Home Marketing.

Q. How did you know that, uh, this worksheet for manual J, Exhibit Number Six, was for the house contracted for by Onilea Neal?

A. It was brought in with the materials.

Q. But, there's no model number on that, it's predated a year before the contract, is that correct?

A. That's correct.

Q. Did you ask any questions about that?

A. No.

Q. Did you check with the state office and see if the manual J had been reviewed and approved by the state office?

[61] A. I did not.

Q. Did you know whether or not, did you find out subsequently that it was approved or inspected by the state office?

A. The only thing that I knew was that these houses issued by Home Marketing model numbers were approved.

Q. But, there's no model number on that worksheet J, is there?

A. Right. No.

Q. Didn't you ask any questions about that?

A. No.

Q. Did you in fact review that document, manual J?

A. I looked at it, saw that it takes a certain amount of heating and cooling.

Q. Didn't you bother to check to see if it was for the same house or not?

A. The square footage of it is, uh, the only thing that I looked at.

Q. And, what is the square footage?

A. I believe it's nine, nine sixty.

Q. Okay. And, what's the square footage on—

A. (interposing) Nine hundred and sixty.

Q. Where is that shown?

A. Now, I may be off on it, but the thousand, her's is nine hundred and twenty square feet.

[62] Q. And, you're referring to the contract, is that correct?

A No.

Q. What are you referring to?

A. Appraisal.

Q. But, is square footage the only, uh, criteria that they use in computing the heat loss capacities of dwellings?

A. That, they chart, got a lot of calculations in it, and I am not qualified to interpret all those.

Q. Don't you receive, didn't you say you receive training on how to read specifications and drawings and charts? Are you telling me right now that you cannot, uh, interpret any of these figures from the J chart?

A. No, I'm not saying I can't interpret any of them.

Q. Okay. What factors are, go into determining the heat loss capacity of a house?

A. The window area, the door area, your interior wall construction, insulation in between the walls, insulation overhead, uh, in the floor, your exterior insulation, your exterior wall covering, all of these items.

Q. Okay. And, my question then is, did you check all these items and compare them between the manual J and the plans to see if they matched up?

A. Because this gives—

[63] Q. I'm talking about the time that they were submitted, and you, you read over it?

A. No.

Q. Did you check and make sure that the same number of windows were computed in the J chart as the plans called for, and that the—

A. (interposing) No.

Q. That the insulation and all was calculated?

A. No.

Q. All you looked at was square feet, right?

A. Basically.

Q. And, there was a difference of square feet in there, wasn't there, between the two houses, right?

A. Yes.

Q. In effect, this house says something about a carport. Did Ms. Neal get a carport?

A. No.

Q. Now, Mr. Parkison, on the plans, uh, they're numbered as Exhibit Number Five, do those plans include any, any drawings or locations for the heating and cooling unit?

A. They do not.

Q. Are drawings and plans required for location and duct work and equipment on heating and cooling?

A. We don't always require them.

[64] Q. I refer you to a regulation, seven CFR, section

eight-oh-four, subpart A, reading on subparagraph B, floor plans, subparagraph nine, heating and system on, heating system on separate drawing or when it may be shown to clearly explain. It may be a part of the floor or basement plan, showing layout of system, location and size of duct, piping, register, radiators, location of heating unit and room thermostat, and total calculated heat loss of the dwelling including heat loss through all vertical surfaces including the floor. It seems that the regulations require it. Are you saying that, that they didn't meet that requirement?

A. I did not have them.

Q. You didn't have any copies of it, is that right?

A. No.

Q. Do you know that there was a drawing submitted in Nashville for it?

A. I do not know.

Q. Did you ever ask for one?

A. I asked for a complete set of—

Q. Plans? What did they send you?

A. I haven't received them.

Q. You never received them?

A. No, sir.

Q. When did you ask for those complete set of plans?

A. I, a long time ago.

[65] Q. Before the construction was completed?

A. It wasn't in regards to any one house. I was asking for a set of all that we might be financing.

Q. My question is, did you ask for a complete set of plans prior to or after the time that Onilea Neal's home was constructed?

A. I don't remember. And, I would guess, if I had to just make a guess on it, that it would have been after.

Q. Regardless, you didn't have a complete set of plans, or, the only set of plans you had while Onilea Neal's home

was being constructed was the plans that we have marked as Exhibit Five, is that correct?

A. That's correct.

Q. And, those plans don't show anything about the heating and cooling system, do they?

A. That's correct.

Q. Okay. And, as far as you know, you never asked for any plans for a heating and cooling system?

A. No.

Supreme Court of the United States

No. 81-1494

JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET AL., PETITIONERS,

v.

ONILEA NEAL

ORDER ALLOWING CERTIORARI. Filed May 24, 1982

The petition herein for a writ of certiorari to the United States Court of Appeals for the Sixth Circuit is granted.

Opposition

Supreme Court, U.S.
FILED
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CLERK

NO. 81-1494

In the

Supreme Court of the United States

October Term, 1981

JOHN P. BLOCK,
Secretary of Agriculture, et al.

Petitioner,

v.

ONILEA NEAL,

Respondent.

ON A PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTION PRESENTED

Respondent elects to restate the question presented: Whether Onilea Neal's complaint states a claim for relief against the Farmers Home Administration for negligent inspection and supervision of the construction of her home built under a loan from the Farmers Home Administration made pursuant to Section 502 of the 1949 Housing Act?

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NO. 81-1494

IN THE SUPREME COURT OF THE UNITED STATES
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Respondent.

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FOR THE SIXTH CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION

The respondent Onilea Neal respectfully requests that this Court deny the petition for writ of certiorari seeking review of the Sixth Circuit's opinion in this case. That opinion is reported at 646 F.2d 1178.

STATEMENT

Onilea Neal is a 54 year old woman who lives alone and who has never been married. She is a low-income resident of Roane County, Tennessee. She has less than a high school education. Miss Neal has not previously owned a home. In 1976 Miss Neal was living in a rented dwelling which was in disrepair and was scheduled to be torn down by

the owner. (C.A.App. 139-140) She began to look for another place to live. Since she was unable to find safe and decent housing to purchase or rent within her financial means, she applied for a Section 502 rural housing loan with Farmers Home Administration ("FmHA") on August 16, 1976. (C.A.App. 139-140) As a rural resident living in sub-standard housing within an area with an acute shortage of safe, decent housing, and as a low-income person with no experience in building or buying a home, Miss Neal epitomizes the kind of person Congress intended to benefit through the Section 502 rural housing loan program administered through the FmHA.

FmHA is an agency of the United States Department of Agriculture. It administers Title V of the 1949 Housing Act, as amended, which has the stated national goal of providing a "decent home and suitable living environment for every American family." Under Title V Congress established several loan and technical service programs for rural low-income residents. The relevant provisions of the 1949 Housing Act authorize the Secretary of Agriculture to extend financial and technical assistance, through FmHA, to eligible rural residents in order to provide them "decent, safe and sanitary living conditions." 42 U.S.C. § 1471(a). Financial assistance, in the form of loans for single family owner resident homes, is authorized under § 502 of the 1949 Housing Act, 42 U.S.C. § 1472. Technical assistance is authorized under § 506, 42 U.S.C. § 1476 (emphasis added):

> (a) In connection with financial assistance authorized in this subchapter, the Secretary shall require that all new buildings and repairs financed under this subchapter shall be substantially constructed and in accordance with such building plans and specifications as may be required by the Secretary. Buildings

> and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary. In addition to the financial assistance authorized in this subchapter, the Secretary is authorized to furnish, through such agencies as he may determine, to any person, including a person eligible for financial assistance under this subchapter, without charge or at such charges as the Secretary may determine, technical services such as building plans, specifications, construction supervision and inspection, and advice and information regarding farm dwellings and other buildings.

To be approved for a Section 502 rural housing loan, Onilea Neal (and all other applicants) had to establish that she was unable to obtain credit from any other source on terms she could reasonably be expected to meet. She had to be without adequate housing, but had to have sufficient income to provide for herself and meet all other financial obligations. 42 U.S.C. § 1471(c).

The Section 502 rural housing loan program differs from other government housing programs because of FmHA's involvement in all operations of the program. In other programs, the government plays an important but secondary role to the private lender with whom the borrower has exclusive dealings. In the Section 502 rural housing loan program the borrower deals only with a government employee, known as the county supervisor.[1/]

1/ The organization of FmHA is unique among federal agencies. Unlike the Department of Housing and Urban Development (HUD) which has only a regional organization at the lowest level, the FmHA has 2,200 county offices which are supervised by district offices and coordinated by a director for each state. HUD employees never become personally involved in the loan process under HUD administered housing program. Applicants who wish to participate in HUD home loan insurance programs first apply to a HUD-approved private mortgage lender, which in turn applies to HUD. Applications for loans from the FmHA are made directly with employees at the 2,200 local county offices. The United States Government Manual 1981/82, pp. 105, 107.

The FmHA county supervisor determines eligibility for a Section 502 rural housing loan. 7 C.F.R. § 1822.11(b) (1977).[2/] The county supervisor checks a borrower's credit information. 7 C.F.R. § 1822.11(a)(2) (1977). Prior to a borrower purchasing a home site

> The County Supervisor should . . . advise him [borrower] with respect to the size, design, quality, cost and location of the dwellings and dwelling sites suitable for the [Section 502 rural housing] program.

7 C.F.R. § 1822.11(d) (1977). The county supervisor reviews the borrower's proposed plans and specifications for compliance with minimum property standards. 7 C.F.R. § 1804.3(d) (1977). The county supervisor prepares all loan documents. 7 C.F.R. § 1822.12-15 (1977). Even title clearance and legal services are provided to the borrower through the county supervisor. 7 C.F.R. § 1822.9(d) and Part 1807 (1977). The county supervisor disburses loan proceeds. 7 C.F.R. Part 1803 (1977); 7 C.F.R. § 1822.14 (1977). After the loan is completed and the construction finished, the county supervisor continues to service the borrower's account with FmHA. 7 C.F.R. Part 1861, Subpart A (1977).

The FmHA county supervisor is to provide further supervisory assistance to the borrower.

> Supervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect

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2/ FmHA cites 1980 regulations and implies that these regulations were "in effect at all times relevant to this case." (Pet. p. 4) This simply is not correct. See Pet. p.5, n.1. The regulations cited by respondent will be the regulations effective between August 16, 1976 and October 3, 1977, when Miss Neal applied for a Section 502 rural housing loan and when her home was completed. (C.A.App. 140, 162)

> the interests of the Government in accordance with Subpart A of Part 1802 of this Chapter.

7 C.F.R. § 1822.7(a) (1977).

> The basic objective of the Farmers Home Administration (FmHA) in making section 502 loans is to assist farmowners and other persons who will live in rural areas to obtain decent, safe, and sanitary dwellings and related facilities.

7 C.F.R. § 1822.2 (1977).

> The primary objectives of supervision are to assist . . . families to . . . obtain decent, safe, and sanitary housing . . . .

7 C.F.R. § 1802.2(b) (1977).[3/] This supervision requires the FmHA county supervisor's close involvement in the planning and construction of the housing, including inspection of the construction.

> The County Supervisor will inspect development work as frequently as necessary to assure that construction and land development conforms with the plans and specifications.

7 C.F.R. § 1804.4(g)(3) (1977).

Onilea Neal's application was approved on June 9, 1977 and she was determined eligible for a Section 502 rural housing loan of $21,170. (C.A.App. 142-143) After consultation and counseling with Miss Neal, S. Lane Parkison, FmHA County Supervisor for Roane County, Tennessee, suggested that she buy a modular home "because the house that she was living in was falling down" and that she needed "immediate housing." (C.A.App. 122) He referred her to three

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3/ Regulations further provided that "[s]upervisory assistance is especially important with families receiving initial Farmers Home Administration loans who are relatively inexperienced. . . ." 7 C.F.R. § 1802.65 (1977).

modular home builders, including Home Marketing Associates, Inc. (hereinafter referred to as "Home Marketing"). She entered into contracts with Home Marketing for the construction of a modular house, Model 3B-1000B, financed by FmHA. (C.A.App. 28-32) The contracts specified that the construction was to conform to FmHA approved plans and specifications; that changes in plans and specifications were not to be made by the contractor and borrower without the written approval of FmHA; and that FmHA was to inspect, examine and test all materials and workmanship and had the right to reject any defective materials and workmanship or to require its correction.

As required by regulation, Home Marketing submitted to FmHA plans and specifications for Model 3B-1000B which purported to be for Miss Neal's dwelling. 7 C.F.R. Part 1804, Subpart A, Appendix C (1977). The plans for Model 3B-1000B did not include any layout of a heating and cooling system. (C.A.App. 148-152) However, specifications listed in "Descriptions of Materials" identified the heating system as electric, "General Electric, 220 Volts, output 15kw-Btuh," and identified the cooling equipment as "central system 2 ton air conditioner 15 kw." (C.A.App. 146)

Mary C. Wells, Assistant Roane County Supervisor for FmHA, made inspections during construction of Miss Neal's home. The reports indicated that inspections took place when the home was 2% completed (on August 24, 1977), 99% completed (on September 19, 1977), and 100% completed (on October 3, 1977). (C.A.App. 159-163) All inspection reports were signed by Mary Wells. Miss Neal did not sign the first two inspection reports and there is no indication that she was given a copy of any of the inspection reports.

Nothing was noted on the reports except for the comment "Footings ok" on the first report.

The inspection reports were not appraisals. The inspection form (FmHA 424-12) required the FmHA official to "itemize and describe the significant conditions observed to be at variance with the approved plans and specifications" and make "recommendations for correcting the deficiencies." If deficiencies were previously reported, the FmHA was to check to see if they had been corrected. To assist the FmHA inspector, the inspection report form contained a checklist guide on the back. (C.A.App. 159-160)

Once the house was completed, Onilea Neal executed a promissory note secured by deed of trust in favor of FmHA for repayment of the loan amount. (C.A.App. 33-39) As required by FmHA, Home Marketing executed a one-year builder's warranty which promised that the building was constructed in conformance with drawings and specifications approved by FmHA and minimum property standards published by the Department of Housing and Urban Development. The warranty applied to all workmanship, materials, and installation of equipment, including the heating system. The warranty specifies the installation of a Chrysler heat pump, serial number 74152PS. (C.A.App. 41)

On December 29, 1977, Onilea Neal notified FmHA and Home Marketing in writing that her heating system was not working. She had not received a warranty booklet or any instructions on the operation of the heat pump, and the name plate on the heat pump had been removed. (C.A.App. 14) In January, 1978, Home Marketing informed Miss Neal that the heat pump unit installed in her home was manufactured by McGraw-Edison. (C.A.App. 14) In February, 1978, FmHA

county supervisor Parkison discovered a tag inside the heat pump unit indicating a sizing of 10kw and 240 volts. In March, 1978, the county supervisor, after having consulted with FmHA officials in Nashville, Tennessee, declared that the unit was defective or undersized and requested Home Marketing to replace the unit. (C.A.App. 15)

On March 22, 1978, Earl Wayne Avery, FmHA State Director for Tennessee, and other FmHA officials inspected Onilea Neal's dwelling. In a letter to Home Marketing dated March 29, 1978, state director Avery confirmed that the heating and cooling system was defective, enumerated additional defects and requested their correction:

1. Porches were constructed of wood in lieu of masonry as shown on plans.

2. Rear service door was not exterior door with lights as shown on plan but appeared to be an interior hollow core without glass.

3. Vertical chase between bath and bedroom was not firestopped or sealed.

4. Bath was rearranged from plan.

5. No grade marks were observed on floor joist or roof truss lumber as required by MPS [Minimum Property Standards of HUD, adopted by regulation for use in FmHA construction.]

6. Roof truss does not appear to comply with approved design submitted with plan, staples used in lieu of nails. Truss design must conform to HUD Criteria for trussed roof structure, 4950.2. The roof had a wavy appearance.

7. The unit was not properly caulked per MPS.

8. The exterior paint appeared to be of a low quality latex and was observed to be flaking off.

9. There was a broken floor joist under the front center bedroom.

10. The plumbing workmanship was observed to be poor.

11. The HVAC unit was observed to be a heat pump with 9.2 KW of auxiliary heater strips. Specifications called for General Electric 2 ton air conditioner and 15 KW of electric heat. Manufacturer of equipment could not be determined.

12. 1" x 3" bridging [between floor joints] was not observed, as shown in specifications.

13. Specifications call for 1/2" sheetrock interior wall finish. Observed was approximately 1/8" plywood paneling. This results in a wall assembly that does not meet MPS fire resistance ratings and span requirements for interior wall finish.

14. The manufacturer failed to certify that the unit was manufactured per approved plans and specifications, MPS and Structural Engineering Bulletin as required per approval letters.

(C.A.App. 43-44)

On December 28, 1979, over two years after Home Marketing and FmHA failed or refused to correct the defects, Onilea Neal filed suit against the Department of Agriculture,[4/] the FmHA, and individual employees of FmHA together with the construction company and individual officers.

Onilea Neal commenced this action in the Circuit Court of Roane County, Tennessee, claiming damages caused by the negligent inspection and supervision of construction of her home by FmHA.[5/] The United States removed the case to the United States District Court for the Eastern District of Tennessee, Northern Division.

4/ Miss Neal filed her administrative claim pursuant to the Federal Tort Claims Act (FTCA), 28 U.S.C. 2671 et seq., on June 6, 1979. The office of General Counsel for the Department of Agriculture did not act upon the claim until January 9, 1980, after commencement of Miss Neal's action against FmHA on December 28, 1979.

5/ When she filed the action, the elderly Miss Neal had lived in the house for two summers without air conditioning and was entering her third winter without an adequate source of heat.

On February 5, 1980 the United States filed a motion to dismiss the claims against the federal defendants for lack of subject matter jurisdiction and for failure to state a claim upon which relief could be granted. Miss Neal filed response to the motion to dismiss on February 12, 1980. Also on February 12, 1980, Miss Neal filed an amended complaint to allege federal jurisdiction more specifically.

On February 26, 1980, the district court entered an order dismissing the claims against the federal defendants holding that the "plaintiff has failed to state facts upon which relief from the government defendants can be based."[6/] Neal v. Bergland, et al., 489 F.Supp. 512, 516 (E.D.Tenn. 1980), reversed, 646 F.2d 1178 (6th Cir. 1981). (Pet. p. 26a)

Onilea Neal appealed the judgment of the district court to the Sixth Circuit Court of Appeals. The court of appeals reversed the judgment of the district court holding that Onilea Neal had stated sufficient facts of negligent supervision and inspection of the construction of her home to establish a claim for relief against the federal defendants. Neal v. Bergland, et al., 646 F.2d 1178 (6th Cir. 1981). (Pet. pp. 4a-18a)

6/ FmHA errs in asserting that the district court dismissed Miss Neal's complaint "for lack of subject matter jurisdiction." (Pet. p. 7) Furthermore, it should be noted that the district court made its ruling without benefit of the depositions of Wayne Humphrey (Home Marketing), S. Lane Parkison (FmHA county supervisor) and Mary C. Wells (FmHA assistant county supervisor) taken on February 7, 1980, and February 22, 1980. (C.A.App. 104, 116, 124) Mr. Humphrey's deposition was filed with the district court on February 27, 1980. The depositions of S. Lane Parkison and Mary C. Wells were filed on March 7, 1980. (C.A.App. 3) The claims against Home Marketing were remanded by the district court to the Roane County, Tennessee, Circuit Court where the case is presently awaiting trial. Home Marketing is no longer constructing homes and has been suspended from participating in FmHA rural housing programs.

This Court should be aware that several of the defects cited in Miss Neal's complaint have been corrected at FmHA's expense since this litigation began. FmHA paid for repair of faulty plumbing and for replacement of the heating and cooling system in October, 1980 (a fact reported to the court of appeals during oral argument in December, 1980). By March 5, 1982, FmHA paid to reconstruct interior walls (which failed to meet minimum fire standards) and to repair several other defects. These repairs alone totaled $9,010.34, almost half Miss Neal's original loan.

These repairs were completed only after more than three years of effort directed at FmHA. Correspondence and proceedings leading up to the completion of these repairs, and FmHA's refusal to correct other deficiencies are not part of the record. The record does not establish whether FmHA's agreement to correct certain deficiencies arose out of a determination pursuant to its construction defect program (42 U.S.C. § 1479(c)) or as a result of this litigation, or for some other reason.[7/] At any rate, Miss Neal complained of other deficiencies which have not been corrected and she suffered other damage for which she has not yet been compensated.

SUMMARY OF ARGUMENT

The court of appeals reversed the district court's dismissal of Onilea Neal's complaint for failure to state a claim for relief against the Farmers Home Administration (FmHA) for negligence. It reviewed the allegations in Miss

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7/ FmHA has reported to this Court that "Indeed, respondent sought such relief [under FmHA's construction defect program], but it was denied, presumably because the defects were not substantial." (Pet. p. 14, n.7) Either this statement is an admission that payment was not made pursuant to § 1479(c), or it is an error.

Neal's complaint and the facts and circumstances disclosed by discovery which were in the record. Following the standards set forth by this Court in Conley v. Gibson, 355 U.S. 41 (1957), the court of appeals held, "It does not appear beyond doubt 'that plaintiff can prove no set of facts in support of [her] claim which would entitle [her] to relief.'" 646 F.2d at 1184, quoting Conley v. Gibson, 355 U.S. 41, 45 (1957). (Pet. p. 18a) The decision below rests upon facts peculiar to the case and rests upon the specific language and legislative intent of Title V of the 1949 Housing Act. The decision below conforms with this Court's decision in Indian Towing Company v. United States, 350 U.S. 61 (1955). The petition for a writ of certiorari should be denied.

The sole Question Presented in FmHA's petition (Pet. p. (I)) is whether a suit alleging negligence by an employee of FmHA "is barred by the 'misrepresentation' exception to suits allowed against the United States under the Federal Tort Claims Act, 28 U.S.C. 2680(h)." The heart and substance of FmHA's contention is that since this Court in United States v. Neustadt, 366 U.S. 696 (1961) "construed the 'misrepresentation' exception . . . as barring suits against the United States for failure to discover and disclose defects in houses built with government financial assistance," the court of appeals' decision allowing Miss Neal to go forward with her negligence claim cannot be reconciled with Neustadt. (Pet. p. 9).

This contention is fatally flawed in several respects. The petitioner distorts this Court's holding in Neustadt and cases which follow Neustadt. It fails to distinguish between the National Housing Act of 1934, the

subject of Neustadt, and the Housing Act of 1949, the subject of this case, and ignores legislative history of Title V of the 1949 Housing Act supporting this action. It attempts to apply inappropriately the "misrepresentation" exception to governmental liability to a situation in which a FmHA employee is negligent at the operational level of a governmental activity.

Further, the petition inaccurately presents several facts which are important to the resolution of the question presented in this case. FmHA misstates the facts, both alleged and demonstrated, which are the bases for Miss Neal's negligence claim. The petition mischaracterizes the manner in which FmHA inspects and supervises construction and how FmHA uses this inspection procedure to correct defects identified during construction. If FmHA is disputing the factual bases of Miss Neal's negligence claim, such a factual dispute underscores the correctness of the opinion by the Sixth Circuit Court of Appeals in reversing the district court's dismissal of Miss Neal's action for failure to state a claim.

Although the court of appeal's decision holds that Miss Neal's complaint sufficiently alleges facts under which FmHA may be held liable for its negligence, there has been no trial on the merits. It is premature to rule on whether the evidence which may be presented at trial supports a claim for negligence and on the measure of damages for which FmHA may be held liable.

REASONS WHY THE WRIT SHOULD BE DENIED

1. Congress intended to benefit low-income persons such as Onilea Neal by providing government supervision and inspection of the construction of homes built under the Section 502 housing loan program.

Onilea Neal's complaint alleges substantial damages flowing from the failure of FmHA employees to exercise reasonable care in supervision and inspection of construction of her home. (C.A.App. 18). FmHA contends that the complaint should be dismissed because the FmHA's duties under the Section 502 rural housing loan program, 42 U.S.C. § 1472, which include inspection and supervision of the construction of homes financed by FmHA to insure that they comply with certain standards of quality in materials and workmanship, create no legal liability for failure to exercise reasonable care in their performance under any circumstances. Rather, FmHA claims that it supervises and inspects the construction of homes financed with its loans merely to protect the government's interest. (Pet. p. 5, n.1; p. 10, n.5; p. 11, n.6.) The only authority for FmHA's proposition is language taken out of context from United States v. Neustadt, 366 U.S. 696 (1961), interpreting the legislative history and intent of an entirely different loan insurance program operated by the Federal Housing Administration (FHA) under the Department of Housing and Urban Development.

The distinction between the FHA and FmHA programs arose when Congress recognized that unlike urban areas, rural areas (which have nearly two-thirds of the country's substandard housing) lack the financial institutions and technical expertise needed to finance and improve rural

housing. 95 Cong.Rec. 4716-4717 (1949). Title V of the 1949 Housing Act, 42 U.S.C. § 1471 et seq., established, among other things, several loan and technical services programs. It was passed to ameliorate rural housing conditions in a manner which recognizes the urban/rural distinction. Rep. Robert Jones (Ala.) explained the need for technical assistance during hearings upon Title V of the 1949 National Housing Act:

> I would like to stress the importance of this technical service. Due to poor structures, poor plans, poor workmanship, or the lack of an over-all scheme for house improvement over the years, the remodeled or modernized house is not always convenient or comfortable. Improved plans and planning service, and education to the construction methods and elements of good planning, are very essential and are positively needed.

Housing Act of 1949: Hearings on H.R. 4009 Before the Committee on Banking and Currency, House of Representatives, 81st Cong., 1st Sess. 178 (1949).

To meet the special housing needs of rural communities, Congress created much more than a loan program with traditional means to protect the government's security interest. 42 U.S.C. § 1472(b). Section 506 of the 1949 Housing Act states the congressional intent for the program in a provision which has no parallel in the 1934 National Housing Act:[8/]

8/ FmHA asserts that the "purpose of the requirement of supervision and inspection [of construction] in the 1949 Housing Act is the same as in the 1934 Act." (Pet. p. 10, n.5) However, no provision within the 1934 National Housing Act authorizes the Secretary of Housing and Urban Development or the FHA to make direct loans to low-income persons; and no provision within the 1934 National Housing Act authorizes the Secretary of Housing and Urban Development or FHA to furnish technical assistance including construction supervision and inspection to such borrowers if there were any. FmHA's assertion is spurious.

> In addition to the financial assistance authorized in this subchapter, the Secretary is authorized to furnish, through such agencies as he may determine, to any person, including a person eligible for financial assistance under this subchapter, without charge or at such charges as the Secretary may determine, technical services such as building plans, specifications, construction supervision and inspection, and advice and information regarding farm dwellings and other buildings.

42 U.S.C. § 1476(a). This technical assistance was intended to help fulfill the Congressional commitment of "The realization as soon as feasible of the goal of a decent home and a suitable living environment for every American family, . . . [Including] governmental assistance . . . to provide adequate housing for . . . rural nonfarm families with incomes so low that they are not being decently housed in new or existing housing . . . ." 42 U.S.C. § 1441.

These sections give the Secretary three duties when making loans: First, the housing constructed must be decent, safe and sanitary--to which end the Secretary is authorized to prescribe standards and make inspections; second, the Secretary must protect the government's interest by securing all loans; and third, he is authorized to assist individual borrowers in attaining the objectives of the Housing Act of 1949 by providing them with technical assistance as prescribed in Section 506 (42 U.S.C. § 1476(a)).

FmHA historically viewed the duty to provide technical assistance to be a paramount part of its program. Its regulations state that the program's basic objective is to assist rural persons obtain decent, safe and sanitary dwellings. 7 C.F.R. § 1822.2 (1977). The regulations further require that each borrower will be provided supervision "necessary to achieve the objectives of the loan

and to protect the interest of the Government." 7 C.F.R. § 1822.7(a) (1977). The regulations also require the FmHA county supervisor to conduct regular inspections of any unit under construction to assure that it complies with the approved plans and specifications and other standards prescribed by the Secretary. 7 C.F.R. § 1804.4(g) (1977).[9/] The Act and regulations explicitly state that the objective of this supervision is to assist families to obtain decent, safe and sanitary housing and not merely to protect the government.

9/ In recent regulatory changes, FmHA has attempted to disavow that inspection of construction is intended to benefit the borrower. 7 C.F.R. § 1924.9 (1981). These changes were proposed in the new regulations since "existing statutes provide for these construction inspections to be conducted by FmHA solely to determine adequacy of the FmHA security." 45 Fed. Reg. 39792, June 12, 1980. No statutory provision in Title V of the 1949 Housing Act supports this contention. Also, this position (that inspections are solely to determine adequacy of the FmHA security) directly contradicts the position by FmHA officials who testified in Congressional hearings in 1948 and 1949 concerning enactment of Section 506 of Title V of the 1949 Housing Act. Infra, pp. 19-21. Also, FmHA's regulatory attempt to avoid its obligation to borrowers under the Section 502 rural housing loan program cannot change ex post facto the intent of Congress when enacting Title V of the 1949 Housing Act. Cf., Fletcher v. Housing Authority of Louisville, 525 F.2d 532, 535 (6th Cir. 1975) (legislative action cannot change ex post facto what was the intent of prior legislation). FmHA's attempt to change legislative intent by regulation is invalid and would not withstand careful judicial scrutiny. However, this Court may wish to consider whether a claim based in part on regulations which have not been in effect for several years represents the most appropriate context within which to review the issues raised by petitioner in this case. A future case which arises under the new regulations would be more appropriate.

> [T]he primary objectives of supervision are to assist [borrowers] to . . . obtain decent, safe, and sanitary housing. [emphasis added]

7 C.F.R. § 1802.2(b) (1977).[10/]

The provisions of Title V of the 1949 Housing Act and the regulations promulgated thereunder provide the FmHA borrower (Onilea Neal) with the very elements that the FHA borrower (Mr. Neustadt) lacked in order to sustain an action against the government. Title V of the Housing Act of 1949, and specifically Section 506, was designed to benefit and protect the rural borrowers under the Section 502 rural housing loan program.

FmHA officials affirmed this intent from the beginning of the program. Charles F. Brannon, Assistant Secretary of Agriculture (later Secretary of Agriculture), emphasized to Congress the need for technical assistance including construction inspection and supervision in the rural housing program:

10/ On November 15, 1976, FmHA proposed to amend Subparts A through F of Part 1802 by consolidating, transferring and redesignating these regulations in a new Part 1924. The changes were "proposed to clarify the regulations on management assistance to individual borrowers and to provide for the assistance to better fulfill the particular needs of the borrower and to protect the interest of the Government." 41 Fed. Reg. 50272 (1976). The new regulations designated as Subpart B of Part 1924, 7 C.F.R., were made final on January 24, 1977. 42 Fed. Reg. 4111 (1977). In the revised regulations, the purpose of the supervision by the FmHA county supervisor is "to protect the Government's interest and to assist the borrower in accomplishing the purpose of the loan." 7 C.F.R. § 1924.59(a) (1978) (emphasis added). The FmHA county supervisor is to "determine and select the appropriate method of supervision to be used in assisting each borrower." 7 C.F.R. § 1924.59(b) (1978). Interestingly, the regulatory changes still provided that the supervision provided borrowers was to further the objectives of the loan "in accordance with Subpart A of Part 1802. [1977]." 7 C.F.R. § 1822.7(a) (1978). This would include 7 C.F.R. § 1802.2(b) (1977).

> The farmers . . . would be benefited by the provisions of the act that provide for technical services and research. Section 705, among other things, would authorize the Secretary [reading]:
>
> > to furnish to all persons, without charge or at such charges as the Secretary may determine, technical services such as building plans, specifications, construction supervision and inspection, and advice and information regarding rural dwellings and other farm buildings.
>
> This is an important part of Title VII because millions of farmers would benefit by its terms.

General Housing Acts: Hearings on S. 866 Before the Committee on Banking and Currency, House of Representatives, 80th Cong., 2d Sess. 293 (1948).[11/] Later, Raymond C. Smith, Assistant Chief, Bureau of Agriculture Economics, Department of Agriculture, again emphasized:

> The bill provides for several types of assistance to farmers. All farmers who desire to obtain better housing would be eligible to benefit by the provisions for technical and educational services and research. Under section 405 [of S. 138] the Secretary of Agriculture . . . would be authorized to furnish all persons . . . technical services such as building plans, specifications,

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11/ Assistant Secretary Brannon's testimony concerned Section 705 of Title VII of S. 866. This provision was favorably acted upon by the Senate in passage of S. 866. The House Committee on Banking and Currency favorably reported a substantially similar bill (H. Rept. No. 2340, 80th Cong., 2d Sess.). Both bills expired at the end of the Eightieth Congress without having reached a vote in the House of Representatives. S. Rep. No. 84, 81st Cong., 1st Sess.; reprinted in 1949 U.S. Code Cong. Serv. 1550, 1554-1555. The unfinished and unenacted portions of S. 866, including the provisions for the rural housing program, were the basis for provisions of the 1949 Housing Act. In 1961, Congress extended the provisions of Title V of the 1949 Housing Act to include low-income rural residents. Pub.L. 87-70, § 803(a).

construction supervision and inspection, and advice and information regarding rural dwellings and other farm buildings.

General Housing Acts: On S. 138 Before the Subcommittee of the Senate Committee on Banking and Currency, 81st Cong., 1st Sess. 209 (1949).[12/]

If Congress had intended the Section 502 rural housing loan program to be merely an extension of the FHA loan insurance program under the Department of Housing and Urban Development, it would not have had to pass new legislation and enlarge the duties of an agency under a different department. Congress, however, took a new approach to the housing problem in rural communities and designed a program to stimulate and provide quality home construction. Legal rights and duties established in the first statutory scheme are simply not applicable to the newer program. Neustadt does not govern the decision by the court of appeals in this case.

2. Neustadt does not bar suits for negligent inspection and supervision of construction of a home built under the FmHA Section 502 rural housing loan program.

FmHA states: "In Neustadt, the Court construed the 'misrepresentation' exception to the Federal Tort Claims Act, 28 U.S.C. 2680(h), as barring suits against the United States for failure to discover and disclose defects in houses built with government financial assistance."

12/ Assistant Chief Raymond Smith's testimony before the Subcommittee for the Senate Banking and Currency Committee concerned Section 405 of S. 138. A substantially identical provision was enacted by the 81st Congress as Section 506 of Title V of the 1949 Housing Act. S. Rep. No. 84, 81st Cong., 1st Sess.; reprinted in 1949 U.S. Code Cong. Serv. 1550, 1551.

(Pet. p. 9). The government gives no specific cite for this "holding" in Neustadt. There is a simple explanation of why no citation is given: This was not the holding of Neustadt.

The holding of Neustadt is very narrow: A purchaser of a home was not intended to be a beneficiary of, and therefore cannot rely upon, a FHA appraisal made for issuance of an insurance commitment to a private mortgagee. A claim against the United States by a purchaser of a defective home with a private mortgage insured by FHA is based upon a misrepresentation--negligent or willful--from which the United States is immune by reason of 28 U.S.C. § 2680(h). 366 U.S. at 708-11.

In Neustadt, the plaintiff, an attorney, purchased a 16 year old home with a private mortgage loan insured by the Federal Housing Administration (FHA) pursuant to Section 203 of the Housing Act of 1934 (12 U.S.C. § 1709).[13/] In connection with its issuance of a conditional insurance commitment to the private lender,[14/] FHA made an inspection of the property to determine whether it was eligible for FHA mortgage insurance and to assign an appraised value establishing the maximum amount of mortgage insurance obtainable. 366 U.S. at 697. Finding no obvious defects and fixing an

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13/ Section 203 of the National Housing Act of 1934, as amended, 12 U.S.C. § 1709, provided that the "[Federal Housing Commissioner] is authorized, upon application by the mortgagee, to insure as hereinafter provided any mortgage offered to him [Commissioner] which is eligible for insurance as hereinafter provided, and, upon such terms as the [Commissioner] may prescribe, to make commitments for the insuring of such mortgages prior to the date of their execution or disbursement thereon . . . ." [Emphasis added.]

14/ An application for FHA mortgage insurance may be made only by a financial institution approved as a mortgagee by the FHA. Section 203(a), National Housing Act of 1934, 12 U.S.C. § 1709(a).

adequate value on the property, FHA issued an insurance commitment, and pursuant to 12 U.S.C. § 1715q, the seller of the home provided Mr. Neustadt with a copy of the appraisal. Several days after Mr. Neustadt took possession of the property, the foundation began to settle in an unusual manner, causing substantial damage to the interior and exterior walls.[15/] 366 U.S. at 698-99.

Mr. Neustadt claimed that he had relied on the FHA appraisal in purchasing the house and commenced a negligence action against FHA, seeking to recover the difference between the market value of the damaged house and the FHA appraised value. 366 U.S. at 701. The issue before the Court was:

> [W]hether the United States may be held liable, . . ., to a purchaser of residential property who has been furnished a statement reporting the results of an inaccurate FHA inspection and appraisal, and who, in reliance thereon, has been induced by the seller to pay a purchase price in excess of the property's fair market value.

366 U.S. at 697-698.

In ruling against Mr. Neustadt on this narrowly drawn issue, this Court rejected the court of appeals' interpretation of Section 226 of the National Housing Act of 1934 (12 U.S.C. § 1715q)[16/] as giving rise to a specific governmental duty to protect prospective home purchasers by

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15/ The cause of the damage to the house which the Neustadts purchased could not be ascertained by inspection of building repair contractors. Only after the original builder and four FHA field inspectors made a core drilling through the basement concrete floor, was it discovered that the subsoil conditions were causing the damages to walls and ceilings. 366 U.S. at 700.

16/ Section 226 of the National Housing Act of 1934, 12 U.S.C. § 1715q, requires a builder or seller to deliver a copy of the FHA appraisal to the prospective purchaser prior to sale.

requiring a careful appraisal by FHA. 366 U.S. at 705. This Court carefully examined the legislative history of the National Housing Act of 1934, especially Section 226, (12 U.S.C. § 1715q), which required that a copy of the appraisal be given to the home purchaser. It found that Section 226 was not meant to protect the prospective homeowner. 366 U.S. at 708. The Court concluded that "the primary and predominant objective of the appraisal system was the 'protection of the Government and its insurance funds.'". 366 U.S. at 709. Since the Court could find no other basis which would give rise to a governmental duty to Mr. Neustadt, his claim based on reliance upon an inaccurate FHA appraisal was barred under the "misrepresentation" exception to the FTCA.

Although the holding of Neustadt is narrow and limited to its facts and statutory context, the analysis by the Court in Neustadt has been useful in other cases to determine whether a duty is owed to a plaintiff injured by the negligence of government employees. More importantly, the approach to the issue taken by this Court in Neustadt--the careful examination of the specific statute in question, and its legislative history--in fact guided the court of appeals in this case.

The government seeks to avoid this analysis by asserting that the present case "is identical to Neustadt." (Pet. p. 12) It mischaracterizes this case. Neustadt dealt with governmental actions under the FHA mortgage insurance program under the National Housing Act of 1934. The present case arises out of the actions of local government employees under the FmHA rural housing loan program of the Housing Act of 1949. The court of appeals observed:

> Although Title V focuses on financial assistance, S.Rep. No. 84, 81st Cong., 1st Sess. 2, reprinted in [1949] U.S. Code Cong. Serv. 1550, 1576, Congress has also provided for research and technical services 'pointed toward more efficient and more economical construction' of homes and related structures. Id.
>
> . . .
>
> Thus while it may be said that the overall objective of the loan program is to provide rural residents an opportunity for decent, safe, and sanitary housing, it is to be noted that Congress has specifically authorized FmHA to provide technical assistance and supervision of construction.

646 F.2d at 1180-81 (emphasis added). (Pet. p. 9a). The court of appeals concluded that "Congress, we believe, intended plaintiff [Miss Neal] to be the beneficiary of the inspection and technical assistance offered by FmHA given the purpose of the [1949 Housing] Act and plaintiff's particular circumstances."[17/] 646 F.2d at 1184. (Pet. p. 17a) To assert, as does FmHA, that the plain language and legislative history of Title V of the 1949 Housing Act show no intent to benefit borrowers by specifically authorizing FmHA to provide construction supervision and inspection begs reason. To contend that the injuries which resulted from FmHA's negligent inspection were caused by

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17/ FmHA contends that this conclusion by the court of appeals is contrary to its dismissal of Miss Neal's contract claim. (Pet. p. 11, n.6) The court of appeals found that "no contractual obligation existed on the part of FmHA to provide technical assistance or to supervise construction or to inspect." 646 F.2d at 1181. (Pet. p. 11a) The court goes on to find that once FmHA undertook to provide supervision and inspection of the construction of Miss Neal's home it had a duty to supervise and inspect with due care to protect Miss Neal--"the beneficiary of the inspection and technical assistance offered by FmHA." 646 F.2d at 1184. (Pet. p. 17a) The denial of Miss Neal's contractual claim does not contradict the finding that FmHA voluntarily undertook construction supervision and inspection and owed Miss Neal a duty to inspect and supervise with due care because she was the beneficiary of such inspection and supervision.

some "misrepresentation" to Miss Neal ignores the clear allegation in the complaint and the factual evidence in the record.

3. Onilea Neal's complaint alleges damages resulting from FmHA's negligent inspection and supervision of construction.

Onilea Neal's negligence claim is not predicated upon a "misrepresentation" by government employees--willful or negligent.[18/] Miss Neal's claim is that by negligently inspecting and supervising the construction of her home, FmHA authorized payment to the contractor for work he did not perform or for work the contractor performed contrary to plans and specifications approved by FmHA, and authorized occupancy of the defective house contrary to the statute and regulations governing the Section 502 rural housing loan program.

The FmHA county supervisor is a "one-stop housing center" for rural residents. Under the Section 502 rural housing loan program, he determines program eligibility, reviews proposed house plans and costs, checks the borrower's credit, executes the loan documents, makes construction inspections and disburses the loan proceeds. Once the loan is completed, he services the loans by collections and, if necessary, counseling. Supra, pp. 4-5. In short, he carries out all the functions of a private mortgagee and technical consultant. From the borrower's and

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18/ 7 C.F.R. § 1804.4(g) (1977) did not require, or even suggest, that copies of the inspection reports (FmHA 424-12) to be given to borrowers. Neither does the present "version" of the construction inspection regulation, 7 C.F.R. § 1924.9 (1981). There is no statutory provision within Title V of the 1949 Housing Act which requires that copies of reports of construction inspection and supervision by FmHA be given to borrowers.

builder's vantage, the FmHA loan is a direct loan from the government.

In this case, the county supervisor and contractor understood the statutory objective of the Section 502 home loan program and the purpose of supervision and inspection of construction.

> Q. [Croce] What's the objective of the section five-oh-two homeowner's loan program?
>
> A. [FmHA County Supervisor] The objective is to provide decent, safe and sanitary housing to meet the needs of rural residents.

(C.A.App. 120).

Similarly, the FmHA county supervisor perceived his duties of supervision and inspection of construction as an integral process in achieving the objectives of the Section 502 home loan program:

> Q. And, let me ask you this, Mr. Parkison, Uh, don't you think some of these things, like inspections and warranties, contribute toward that objective?
>
> A. It's part of the, part of the loan process.
>
> Q. Uh-huh. If the objective is to assure that people that, uh, in rural areas, to assure that they get safe, decent and sanitary housing, then part of the objective for making inspections and requiring warranties, and, you know, if there's something wrong, that you can withhold the money, and stuff like that, is to make sure that in fact those borrowers do get safe, decent and sanitary housing, is that correct?
>
> A. That's correct.

(C.A.App. 120-121).

Thus, if during construction, the contractor desires a partial payment, FmHA inspects the construction and either

approves or disapproves payment. Before the contractor may be paid, a FmHA official must authorize payment.[19/] (C.A.App. 119). FmHA is simply wrong to assert that injury would not have occurred to Miss Neal unless information concerning the inspection was conveyed to her. (Pet. p. 12) The county supervisor's admissions show that he was aware that if defects had been discovered by a proper inspection, payment to the contractor would not have been authorized.

The contractor in this case also recognized that the inspections by the FmHA county supervisor are to assure that the dwelling is constructed in accordance with plans and specifications, and that correction of defects does not depend upon any representation to the borrower.

19/ FmHA has two procedures for disbursement of loan funds: the loan disbursement system (LDS) and the use of supervised bank accounts. 7 C.F.R. Part 1803 (1978). Under the LDS, the county supervisor requests that the FmHA finance office issue a check in an amount determined by the county supervisor. The check, made payable to the borrower, is delivered directly to county FmHA office where the county supervisor checks the name of the borrower and amount and places a restrictive endorsement upon the check to insure proper payment. 7 C.F.R. § 1803.3 (1978). Under a supervised account, the amount of the entire loan is requested by the county supervisor and deposited in a bank account requiring two signatures, the borrower's and a FmHA official. 7 C.F.R. §§ 1803.4 and 1804.8 (1978). Checks drawn on supervised accounts will be countersigned by the county supervisor "only if the quantity and quality of items purchased are in accordance with approved plans." 7 C.F.R. § 1803.8(d)(3)(i) (1978). Supervised accounts are to be used in rare occasions. Among reasons for using supervised accounts are "to assure the correct expenditure of all or a part of loan and grant funds" and to help the borrower who does not show ability to manage his financial affairs to learn personal financial management. 7 C.F.R. § 1803.2(a)(4) and (6) (1978). Disbursement of Miss Neal's Section 502 rural housing loan funds were made through a supervised bank account.

Q. [Croce] So, if Farmers Home Administration isn't satisfied with either the amount of work done, or the quality or manner in which the work is done, then they'll either not pay or they'll withhold a certain portion that check, is that correct?

A. [Contractor Humphrey] That would be my understanding, yes.

(C.A.App. 110).

FmHA asserts that the gravamen of Miss Neal's complaint is that "the government was negligent in not discovering the defects and disclosing their existence to her." (Pet. p. 10) This characterization of her claim is incorrect and ignores the record below and the specific findings by the court of appeals. Her complaint is not based on failure to disclose or misrepresentation. The facts and allegations in the complaint show that FmHA undertook inspection and supervision of the construction of Miss Neal's home. It FmHA's inspection had been done properly and with due care, FmHA could have prevented injury to her by withholding funds from the contractor until the defects were corrected.

To achieve the purpose of supervision and inspection FmHA need not make a representation of any kind to Miss Neal or any other borrower and Miss Neal has not claimed that a misrepresentation was made. Indeed, if FmHA had discovered the defects in her home during construction and had responded only by telling her about them, such a response would be an abdication of its responsibility under the rural housing program. It is inconceivable that Congress would specifically have authorized FmHA to supervise and inspect construction of homes for its low-income, inexperienced borrowers and then expect them to be solely responsible, upon notice, for correcting construction defects. The

entire scheme of construction inspection and supervision requires that FmHA do something when it discovers defects during construction.

Once it undertook construction inspection and supervision, FmHA's duty to Miss Neal was to use due care in making inspections to assure that her home was built in conformance with plans and specifications. Miss Neal's claim is that FmHA breached this duty by not using due care in making construction inspections which resulted in damages to her.

4. Given the particular facts and allegations presented by Onilea Neal, the Sixth Circuit properly held that its decision was controlled by Indian Towing Company.

FmHA mischaracterizes the factual basis of Miss Neal's claim in an apparent attempt to avoid the distinction which the federal courts have made in holding the United States liable when "the gravamen of the action is not misrepresentation but the negligent performance of operational tasks, although such negligence consist[s] partly of a failure of a duty to warn." United Air Lines, Inc. v. Weiner, 335 F.2d 379, 398 (9th Cir. 1964), cert. dismissed, 379 U.S. 951 (1964).

In United Air Lines, Inc. v. Weiner, the circuit court held that the government officials' negligent failure to inform United of training flight procedures of jet fighters at altitudes customarily used by commercial passenger planes did not fall within the misrepresentation exemption from the Tort Claims Act. Similarly, an F.A.A. air controller's negligent failure to convey weather information to a flight crew constituted "the negligent

performance of operational tasks, rather than misrepresentation." Ingham v. Eastern Air Lines, Inc., 373 F.2d 227, 239 (2d Cir. 1967), cert. denied., 389 U.S. 931 (1967).

In Ingham, as in this case,

> the government's reading of the misrepresentation exception is much too broad for it would exempt from tort liability any operational malfunction by the government that involved communications in any form.

Ingham v. Eastern Air Lines, Inc., 373 F.2d at 239. The negligent inspection of the construction of Miss Neal's home by an employee of the FmHA constitutes negligence at the "'operational level' of governmental activity." Indian Towing Company v. United States, 350 U.S. 61, 64 (1955). Since Miss Neal's claims cannot be distinguished from Indian Towing, Weiner, or Ingham, she should be allowed to proceed with her action on the merits.[20/]

This result does not "muddy" the case law surrounding the "misrepresentation" exception developed by the circuits since Neustadt. Unlike Neustadt and other cases alleging negligence claims arising under the National Housing Act of 1934, and in particular the FHA insured loan

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20/ Once FmHA undertook to supervise and inspect the construction of Miss Neal's home and engendered reliance on its supervision and inspection, FmHA was obligated to use due care in its supervision and inspection of construction. Cf., Indian Towing Company v. United States, supra at 69 (once Coast Guard undertook operation of lighthouse and engendered reliance on the guidance afforded by lighthouse, it must use due care to discover defects and to repair or to warn). Tennessee courts recognize this "good Samaritan" rule of tort law: "It is ancient learning that one who assumes to act, even though gratuitously, may thereby become subject to the duty of acting carefully, if he acts at all." Nidiffer v. Clinchfield Railroad Company, 600 S.W.2d 242, 246 (Tenn.App. 1980), quoting Glanzer v. Shepard, 233 N.Y. 236, 135 N.E. 275 (1922) and citing Prosser, Law of Torts, 4th ed., Limited Duty, § 56 "Acts and Omissions."

program,[21] the Sixth Circuit found that Congress, under Title V of the Housing Act of 1949, "intended plaintiff [Onilea Neal] to be the beneficiary of the inspection and technical assistance offered by FmHA given the purpose of the Act and plaintiff's particular circumstances." 646 F.2d at 1184. (Pet. p. 17a). Cf., Fletcher v. Housing Authority of Louisville, 491 F.2d at 803 n.37 (amendments to Housing Act of 1937 were intended to benefit the very poor by authorizing additional payments to cover operating deficits of local housing authorities); vacated, 419 U.S. 793, reinstated, 525 F.2d 523 (6th Cir. 1975); Thompson v. Washington, 497 F.2d 626, 633 (D.C.Cir. 1973) (in providing for controlled rents, Congress plainly intended to create a benefit in favor of tenants to enjoy subsidized housing at less than market price which includes the tenants' right to hearing prior to approval of rent increases).

The court of appeals also concluded that Miss Neal's negligence claim was not predicated on a reliance upon inspection reports, but that "plaintiff is complaining . . . that FmHA negligently supervised construction and negligently inspected her house." 646 F.2d at 1184. (Pet. p. 18a). Miss Neal's claim is that FmHA wrongly authorized payment to the contractor for shoddy construction which could have been prevented had FmHA employees supervised and inspected the construction of her home with due care. Thus,

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21/ Plaintiffs' claims in Baroni v. United States, 662 F.2d 287 (5th Cir. 1981), and Thompson v. United States, 408 F.2d 1075 (8th Cir. 1969) were dismissed in part, because the courts determined that Congress did not intend to protect prospective home buyers under the National Housing Act of 1934 and regulations thereunder. 662 F.2d at 289; 408 F.2d at 1081. See also, United States v. Thompson, 293 F.Supp. 1307, 1312-1313 (E.D.Ark. 1967).

the negligent misrepresentation exception is inapplicable.[22/] See, e.g., Ware v. United States, 626 F.2d 1278, 1282-1283 (5th Cir. 1980) (The tort of negligent misrepresentation demands some act, the result of justifiably relying on the misrepresentation.).

5. The court of appeals' opinion is consistent with the purpose of Title V of the Housing Act of 1949, as amended.

Despite the differences between the FHA loan insurance program and FmHA rural housing loan program, the principle of Neustadt has been misapplied in decisions concerning claims under the FmHA rural housing loan program. Those decisions fail to follow the approach established by this Court in Neustadt of carefully analyzing the statute and legislative history of the specific housing program in question. Having failed to make this analysis, several courts erroneously applied decisions arising out of one act (such as the National Housing Act of 1934) to a program created by an entirely different act (such as the Housing Act of 1949).

In Adamsville Lumber Company, Inc. v. Rainey, 348 F.Supp. 373 (W.D.Tenn. 1972), the district court stated, in dictum, that "[t]he legislative history of the relevant Acts make it clear that Congress intended to benefit and protect only the Government" (citing United States v. Neustadt, 366

22/ Plaintiffs' claims in City and County of San Francisco v. United States, 615 F.2d 498 (9th Cir. 1980), Preston v. United States, 596 F.2d 232 (7th Cir. 1979), cert. denied, 444 U.S. 915 (1979), Somali Development Bank v. United States, 508 F.2d 817 (Ct.Cl. 1974), and Cenna v. United States, 402 F.2d 168 (3d Cir. 1968), were classic allegations of injury which "resulted from a commercial decision based on a governmental misrepresentation." 596 F.2d at 239.

U.S. 696 (1961)). 348 F.Supp. at 377. This dictum was in the context of a claim by a building contractor asserting that FmHA had a duty to require the home buyer to procure insurance protecting the contractor from loss due to fire before acceptance of the home by the buyer. The court was correct in finding that no provision in the relevant statutes or regulations creates such a duty to the contractor. Cf., M. B. Guran Co. v. City of Akron, 546 F.2d 201, 204 (6th Cir. 1978) (unsuccessful bid of contractor does not give rise to implied right of action since the contractor was not a member of the class of persons who inhabit inadequate housing for whose "especial" benefit the Housing Act of 1949 was enacted). However, the district court's reliance upon this Court's analysis of the Housing Act of 1934 was misplaced. The court here mechanically applied Neustadt's results without carrying out the analysis it held to be required in such cases.

In Ramsey v. Farmers Home Administration, 443 F.Supp. 760 (E.D.Mo. 1978), the court dismissed the plaintiff-homebuyer's claims because it determined that the regulations incorporated into the loan contracts between FmHA and borrowers create no contractual obligation enforceable by the borrower. The district court again mechanically cited Adamsville, supra, (which in turn relied upon Neustadt) for this proposition without discussion of the applicability of the Neustadt analysis of the FHA's § 203 loan insurance program to the FmHA's Section 502 rural housing loan program. This failure to analyze the differences between the two programs renders the dictum in Ramsey v. Farmers Home Administration meaningless.

The Reynolds case, on which FmHA relies as evidence of an alleged conflict among circuits and justification for hearing this case, similarly failed to analyze Neustadt adequately. Reynolds v. United States, 643 F.2d 707 (10th Cir. 1981), cert. denied, No. 80-2064 (Oct. 5, 1981). FmHA mischaracterizes Reynolds as being "in direct conflict with" and "based on virtually identical facts" as the case below. (Pet. p. 15) Although the Sixth Circuit acknowledged in a footnote the suggestion that Reynolds conflicts with Neal, a careful reading demonstrates that it in fact distinguished the two cases:

> Subsequent to the decision in this case the Court of Appeals for the Tenth Circuit released its opinion in Reynolds, et al. v. United States, No. 79-2068 (filed March 9, 1981), which appears to be contrary to our holding above. Careful review suggests that we take a different view of Congressional intent and the purposes of the statute with regard to technical assistance. Here, unlike Reynolds, the damages claimed were the direct consequences of the alleged negligent inspections, i.e., defects in the house. We are satisfied that plaintiff is entitled to go forward with her case.

646 F.2d at 1184, n.7. (Pet. p. 18a)

The plaintiff in Reynolds was not a Section 502 borrower but was an invitee who was injured by an allegedly improperly installed furnace. He was characterized by a later court as a

> 'bystander' who cannot be said to have relied on the expertise of FmHA in the inspection and supervision process, and to whom no duty was owed to make competent inspections. The relationship between his injuries and the negligent inspection was too tenuous to support a claim under the FTCA.

Park v. United States, 517 F.Supp. 970, 978-79 (D.Ore. 1981), appeal docketed, No. 81-3524 (9th Cir. Dec. 11, 1981).

Not only does FmHA fail to recognize the significance, within the context of the Section 502 rural housing loan program, between the "bystander" in Reynolds and Miss Neal, but the court in Reynolds itself failed to recognize the distinction between the FHA program under consideration in Neustadt and the Section 502 rural housing program. The Tenth Circuit also mechanically cited Neustadt for the proposition that the "misrepresentation" exception of the Tort Claims Act applies to all instances of negligent inspections under federal housing programs. Reynolds, 643 F.2d at 711. The circuit court in Reynolds makes the same quantum leap as the district courts in Ramsey v. Farmers Home Administration, supra, and Adamsville Lumber Co. v. Rainey, supra.

The decision by the court of appeals in Ortiz v. United States, 661 F.2d 826 (10th Cir. 1981), is similar in its facts to this case, but it shares Reynold's failure to analyze the statutory context within which FmHA employees undertook inspection and supervision of construction. Although it acknowledged the argument that there were "significant statutory and regulatory differences between the Federal Housing Administration and FmHA," the court of appeals applied Neustadt for the proposition that borrowers under the Section 504 rural housing repair program were not intended beneficiaries of construction inspections by FmHA employees. 661 F.2d at 829-830. The court of appeals cites no statutory provision or legislative history of Title V of the 1949 Housing Act to support this conclusion. Simply stated, Ortiz is wrongly decided and does not follow the kind of analysis undertaken by this Court in Neustadt to

determine when a government employee's negligent actions were undertaken to benefit the plaintiff.

In sum, FmHA does not cite any case or legislative history which supports the contention that Congress intended to benefit and protect only the government when it authorized inspection and supervision of construction of homes financed under the Section 502 rural housing loan program. Rather, FmHA assumes an analogy between the FHA insured loan program and the Section 502 rural housing loan program--an analogy for which there is no support in either the language of the two acts or their legislative histories.

FmHA notes that Congress, in the wake of Neustadt, enacted a fund to correct defects of homes financed under the FHA insured loan program (12 U.S.C. § 1735b(b)). By enactment in 1977 of a similar program for homes constructed with direct FmHA loans (42 U.S.C. § 1479(c)), FmHA contends that Congress recognized the applicability of Neustadt to homes constructed under the Section 502 rural housing loan program. (Pet. pp. 14-15.) FmHA cites no legislative history concerning enactment of Section 502 (42 U.S.C. 1472(a)), Section 506 (42 U.S.C. § 1476(a)), or Section 509(c) (42 U.S.C. § 1479(c)) of the 1949 Housing Act to support the contention.

In fact, the House Report on the 1977 amendments to Title V of the 1949 Housing Act demonstrates that Congress expected FmHA to prevent construction defects in the Section 502 rural housing loan program by inspections and supervision.

> Complaints concerning shoddy construction in some FmHA homes and the inability of FmHA to correct the situation after the fact have come to your committee's attention. Most, if not all, of these instances of shoddy construction could have been

> avoided with proper inspection procedures and appropriate contractual arrangements (such as escrow agreements) with builders. Your committee expects the Secretary to put much greater emphasis on such administrative safeguards so that, as a result, the authority provided in this section [509(c)] will seldom have to be used.

H.Rep. No. 95-236, 95th Cong., 1st Sess., p. 27-28; reprinted in 1977 U.S. Code Cong. & Ad. News 4454-4455. House Report No. 95-236 gives no indication that Congress considered Neustadt when it enacted Section 509(c) (42 U.S.C. § 1479(c)), and certainly none that it intended to adopt its holding. Congress gave no indication that it intended Section 509(c) to be an exclusive remedy as stated in the petition.[23/] (Pet. p. 15).

The circuit court's opinion is consistent with a plain reading of statutes, regulations and legislative history concerning the FmHA Section 502 rural housing loan program. It carefully considered and analyzed the holding in United States v. Neustadt, 366 U.S. 696 (1961) in light

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23/ House Report No. 95-236 reinforces the conclusion that Congress intended the inspection and supervision of construction by FmHA to benefit the borrower by preventing "shoddy construction." FmHA undertook to inspect and supervise the construction of Onilea Neal's home and therefore engendered a reliance upon such inspections and supervision to assure that her home was constructed properly and in accordance with plans and specifications. Such an undertaking, even if gratuitous, gives rise to a duty which must be discharged with due care. A breach of such a duty by negligently inspecting and supervising construction gives rise to a claim under the FTCA. Section 509(c) (42 U.S.C. § 1479(c)) does not portend to supplant remedies under the FTCA and therefore can only constitute an "exclusive" remedy absent a valid claim under the FTCA. Thus, since a purchaser of a home with a mortgage insured under provisions of the National Housing Act of 1934 was not intended to be a beneficiary of appraisals for federal mortgage insurance and therefore was not owed any duty of care by FHA inspectors, he cannot maintain a claim under the FTCA. The purchaser's remedy is restricted to the administrative remedy provided by Congress under Section 518(b) of the Housing Act of 1934, as amended, 12 U.S.C. § 1735b(b). Summers v. United States, 510 F.2d 123, 125 (8th Cir. 1975), cert. denied, 423 U.S. 851 (1975).

of the complaint filed by Onilea Neal. 646 F.2d at 1182-1184. (Pet. pp. 14a-18a) Based upon the allegations and facts presented, the circuit court reached the inescapable conclusion that Miss Neal had sufficiently alleged a claim for negligence and was entitled to her day in court.

In allowing Miss Neal to proceed with her complaint, the court of appeals did not, of course, find that she was entitled to relief. It held only that, within the context of the statute and regulations governing the Section 502 rural housing loan program, her complaint alleged a degree of incompetence and negligence which gives rise to a claim for relief, and that she was entitled to an opportunity to prove that degree of negligence.

It is important to recognize that if the court of appeals' ruling stands, and Miss Neal were to prevail after an ultimate trial on the remaining issues, FmHA should face very little, if any, actual liability. In this case, as in most cases which would arise under Section 502, FmHA stands as a joint tortfeasor with the contractor. FmHA has the opportunity to cross-claim against the contractor and seek to avoid total liability. FmHA can also claim a set-off at trial for the costs of repairs which it has made. 28 U.S.C. § 1346(c). Supra, p. 11. The availability of claims against contractors and setoffs, and FmHA's ability to protect itself through a bond or escrow account, makes FmHA's fear of vast financial liability almost spurious. (Pet. p. 16).

By working with established contractors which are reputable and solvent (which would seem to be required under

the Act), by bonding requirements, or by escrow arrangements, the United States would not be exposed to new or costly payments to its damaged beneficiaries. If Neal has any significant impact on FmHA, it will be to focus the agency more effectively on the true purpose of the Section 502 rural housing loan program. It would perhaps encourage more careful selection of contractors and more careful exercise of its responsibility to inspect and supervise construction.

CONCLUSION

For these reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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Petitioner's Reply Brief

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No. 81-1494

In the Supreme Court of the United States

OCTOBER TERM, 1981

JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET AL.,
PETITIONERS

v.

ONILEA NEAL

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

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In the Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-1494

JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET AL., PETITIONERS

v.

ONILEA NEAL

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

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1. In our petition, we submitted that this case is worthy of review by this Court because the decision of the court of appeals regarding the scope of the misrepresentation exception to the Federal Tort Claims Act, 28 U.S.C. 2680(h), is in conflict with both this Court's decision in *United States* v. *Neustadt*, 366 U.S. 696 (1961), and decisions of the Tenth Circuit in *Reynolds* v. *United States*, 643 F.2d 707, cert. denied, No. 80-2064 (Oct. 5, 1981), and *Ortiz* v. *United States*, 661 F.2d 826 (1981). Respondent attempts to distinguish *Neustadt* and *Reynolds*,[1] but she concedes (Br. in Opp. 35) that *Ortiz*

[1] Respondent's assertion (Br. in Opp. 34) that *Reynolds* can be distinguished on the basis that the plaintiff was an invitee at the house instead of the actual home buyer is spurious. The Tenth Circuit's decision makes no mention of the third-party plaintiff in discussing the FmHA's duty in

"is similar in its facts" and simply asserts that the case was incorrectly decided. Indeed, respondent acknowledges (Br. in Opp. 32) that the weight of judicial authority is contrary to the decision below, but she argues that these cases simply "failed to analyze *Neustadt* adequately" (Br. in Opp. 34). Thus, respondent admits the division of opinion in the circuits and supplies no justification for allowing this conflict to continue. For this reason the petition should be granted.

2. Respondent contends that the decision of the court of appeals is not inconsistent with this Court's decision in *Neustadt* because the statutes involved in the two cases are different. We agree that Section 203 of the National Housing Act of 1934, 12 U.S.C. 1709, at issue in *Neustadt* and Section 506 of the Housing Act of 1949, 42 U.S.C. (& Supp. III) 1476, involved in this case have their differences. But the nature of the statutes, their implementing administrative schemes and common sense all suggest that the differences are immaterial for purposes of the government's monetary liability under the Federal Tort Claims Act, 28 U.S.C. 2671 *et seq.*

Section 506(a) of the Housing Act of 1949, 42 U.S.C. 1476(a), does no more than authorize the Secretary to create a program for inspecting houses constructed with FmHA funds.[2] Nothing in that provision specifies that

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inspecting these houses. It is clear that the Tenth Circuit would have reached the same result if the actual home buyers had been the injured plaintiffs. See *Reynolds* v. *United States*, *supra*, 643 F.2d at 712-713. This, of course, is confirmed by *Ortiz*.

[2] Respondent points out (Br. in Opp. 15 n.8) that in *Neustadt* the FHA guaranteed the loan, whereas here the FmHA actually provides the money for the loan. But in both cases the government's primary concern with regard to inspections was to ensure that its resources were protected. Certainly, a lender has no more concern about construction defects that do not undermine his security interest than does a guarantor.

the inspection is, or should be, for the benefit of the recipient of the loan. Respondent attempts to infer such a purpose from the general statement of purpose of the entire Housing Act of 1949, which is to help provide "decent, safe, and sanitary living conditions." 42 U.S.C. (Supp. III) 1471(a). But nothing in the statute suggests that the *inspection program* is specifically or primarily designed toward that end. Indeed, the legislative history, which we quoted in our petition (Pet. 10 n.5) and which respondent has chosen to disregard, plainly indicates that the purpose of supervision and inspection is to protect the government's security interest. The Senate Report states that "[t]he extent of the requirements for building plans, supervision, and inspection would depend upon the character of the construction and the *amount of the loan.*" S. Rep. No. 84 (Pt. 2), 81st Cong., 1st Sess. 20 (1949) (emphasis added). See also H.R. Rep. No. 590, 81st Cong., 1st Sess. 12, 56 (1949); 95 Cong. Rec. 4764 (1949) (remarks of Sen. Langer). Obviously, an inspection that is dependent on the size of the loan is not designed primarily to benefit the home buyer, but instead is calculated to protect the lender's financial investment. This understanding of the purpose of the inspection has been recognized consistently by the FmHA. Its regulations state explicitly that "supervision" is provided in order "to protect the interests of the Government * * *." 7 C.F.R. 1822.7(a) (1977).[8]

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[8] Respondent attempts (Br. in Opp. 18) to convert a general statement in the regulations (7 C.F.R. 1802.2 (1977)) about the overall purpose of "supervision" into a specific guarantee of "decent, safe, and sanitary housing" to be accomplished through the inspection process. But inspection is not a large part of the supervisor's job and appears not to be at all relevant to the supervisor's effort to provide decent housing. In the regulation describing the County Supervisor's responsibilities for supervision of the home buyer, there is no mention of inspections for defects. In-

Respondent's suggestion that the purpose and structure of the Housing Act of 1949 are fundamentally different from those of the National Housing Act of 1934 is simply incorrect. The latter Act was styled "An act to encourage improvement in housing standards and conditions" (ch. 847, 48 Stat. 1246), thus indicating the same general purpose as in the 1949 Act to protect home buyers. Indeed, the legislative history of the 1934 Act indicates in language much clearer than anything respondent has cited with regard to the Housing Act of 1949 that the FHA's inspection/appraisal provision would benefit the home buyer. Thus, the Conference Report states: "These FHA procedures [inspection and appraisal] also operate for the benefit and protection of the individual home buyer." H.R. Conf. Rep. No. 2271, 83d Cong., 2d Sess. 66 (1954). Nonetheless, this Court in *Neustadt* recognized that the 1934 statute was not designed to create a basis for governmental liability when the FHA inspector failed to discover a defect in the house or, if discovered, failed to take some action to correct it. 366 U.S. at 709-710.

What *Neustadt* teaches is that an inspection program by its nature may create a duty to disclose any defects that are discovered, but that the breach of that duty is not actionable under the FTCA because of the misrepresen-

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stead, the regulation provides for "[t]imely guidance by letter or other means of communications" (7 C.F.R. 1802.3(g) (1977)).

The regulation in effect today is even more explicit in discouraging loan recipients from relying upon the inspection as a guarantee that all construction requirements have been met (7 C.F.R. 1924.9 (1981)). In our view, this change merely clarifies further what already was abundantly clear under the regulations in effect when respondent purchased her home, *i.e.*, that the inspections create no basis for liability. Thus, contrary to respondent's implied suggestion (Br. in Opp. 17 n.9), we do not rely upon the new regulations as a basis for barring her claim.

tation exception (366 U.S. at 700-708).[4] The Court's opinion indicates that an inspection program may give rise to a specific duty created by statute to warrant the quality of the construction. But the opinion also makes clear that Congress must plainly have intended such a result. *Id.* at 708. Other than platitudes about the general purpose of the Housing Act of 1949, respondent has failed to make any kind of showing that "Congress intended, in a case such as this, to limit or suspend the application of the 'misrepresentation' exception of the Tort Claims Act." *Ibid.*

Moreover, respondent's suggested interpretation of the statute defies common sense. On the basis of three relatively brief inspections and the provision of a loan designed to help the needy acquire decent housing, respondent would create an obligation on the part of the government to detect every defect in the house and a duty to refuse to release loan money needed to purchase the house from the contractor until every defect is corrected.[5] Such

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[4] Respondent attempts to avoid the application of the misrepresentation exception by claiming (Br. in Opp. 28) that she did not actually rely upon the inspection report. She did, however, sign the report at the time of the inspection and presumably understood it as an approval of the house as constructed. Moreover, if her claim does not include an allegation of reliance on the government's failure to discover and disclose any defects, then she has no cause of action at all. See *Baroni* v. *United States*, 662 F.2d 287, 289 (5th Cir. 1981), petition for cert. pending, No. 81-1326 (filed Jan. 12, 1982).

[5] For the novel suggestion that the FmHA is required to withhold money on behalf of the home buyer for every defect in the house, respondent cites the deposition of a contractor, who merely indicated that it was his understanding that such action could be taken (Br. in Opp. 28). But the depositions of the FmHA employees make clear that such drastic action would be taken only if the defect were a "really important"

a scheme would impose a burden on the FmHA never intended by Congress[6] and would seriously delay all conveyances under the FmHA rural loan program. Virtually all new houses have "bugs" in them; it is absurd to think that the FmHA must withhold loan money at closing until all such problems are corrected. In the case of non-structural defects that do not jeopardize the government's security interest (see note 5, *supra*), the most that can be expected is that the FmHA generally would inform both the builder and the buyer of the problems it discovers during an inspection.[7] But it is clear that failure

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one (Br. in Opp. 26; C.A. App. 120). This understanding comports with the legislative purpose of the inspection scheme, because major defects are most likely to undermine the government's security interest. Of course, refusal to authorize payment for structural defects would in turn benefit the home buyer, but, as was true with the FHA-insured inspections in *Neustadt*, that protection is a secondary consideration under the statute.

[6] To understand the enormity of the burden respondent would impose upon the FmHA through its inspection process, one need look no further than the list of defects about which she complains. It includes such relatively trivial items as the building material used for the porch, the design of the rear service door, the arrangement of the bath, the absence of markings on lumber used in the house, the "wavy appearance" of the roof, the adequacy of caulking and the quality of the paint (Br. in Opp. 8). It is unreasonable to assume that Congress expected the FmHA inspector to discover these types of defects in every FmHA-financed house and to assume responsibility for having all of them corrected prior to the release of any government funds.

[7] The fact that respondent is poor and not well educated is no basis for assuming, in the absence of express congressional indication, that she is free, based on the inspection, to rely solely upon the FmHA to guarantee the quality of her property. Loan recipients are encouraged to participate in

to notify is exactly what this Court in *Neustadt* held was within the misrepresentation exception to the FTCA. In sum, nothing in the FmHA legislative or administrative materials provides any basis for distinguishing this program from the 1934 Act that was at issue in *Neustadt*.[8]

3. Respondent fails to explain why Congress in 1977 would have enacted an administrative relief program for FmHA loan recipients (see Pet. 13-15) whose houses

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the inspections, and indeed respondent signed the last one (C.A. App. 13-14). Moreover, it is plain that the primary guarantor of the quality of the building is to be the contractor. The regulations make this clear by requiring the builder to issue a one-year warranty on the construction of the house (7 C.F.R. 1804.4(d) (1977)), which the builder did in this case (Pet. App. 6a). Respondent's reliance (Br. in Opp. 27 n.19) on the fact that her account was "supervised" and therefore required co-signing by the County Supervisor as evidence of the FmHA's control over the payment of money pending correction of defects is wholly misplaced. First, most FmHA loans are supervised because most loan recipients, like respondent, are not experienced in handling large sums of money. Second, the supervision is designed to assure that the money is not misused by the loan recipient, not to serve as a basis for holding up payments to the builder pending correction of all defects.

[8] In support of her interpretation of the statute, respondent relies (Br. in Opp. 27 n.19) upon 7 C.F.R. 1803.7(d)(3)(i). That provision deals with the unusual situation where the loan recipient decides to purchase the materials and merely have the contractor come in and work with the materials. The regulation expressly anticipates that money will not be authorized by FmHA for release to pay for the materials unless the materials are approved by the County Supervisor. The regulation has no application to the situation in this case.

have "structural defects" not discovered in the Section 506 inspection, if it had intended those inspections to create a duty to discover and *correct* all deviations from the building specifications that would serve as a basis for liability under the FTCA. Respondent's theory of the FmHA inspection program makes the 1977 amendment completely superfluous.[9] It was only because Congress knew that inspections under its housing loan programs do not create a basis for liability under the FTCA, as interpreted in *Neustadt*, that this administrative remedy was provided.

4. The decision of the court of appeals is plainly inconsistent with *Neustadt* and should be reversed. In light of the extensive submission by respondent in her Brief in Opposition, which relates almost exclusively to the merits of this case and which fails to disclose anything that would create a duty on the FmHA inspector to do more than discover and disclose defects following an inspection—conduct that *Neustadt* clearly exempts under the misrepresentation exception—this case is well suited for summary reversal.

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[9] Respondent is correct (Br. in Opp. 37) that nothing in the legislative materials accompanying the 1977 amendments explicitly refers to *Neustadt*, but she ignores Congress's reliance in 1977 upon the prior enactment of similar relief in the FHA program that had been adopted with *Neustadt* clearly in mind (see Pet. 13-16). The failure to restate that intent in 1977 in no way detracts from the obvious reason why this statute was passed—to provide relief, hitherto not available, for home buyers who relied upon the FmHA inspection program in assuming their house was built properly.

We have been informed by the FmHA that, contrary to our statement in the petition, respondent has received some relief under this program, but apparently not all that she has requested. Of course, the actual availability of this remedy further undermines her claim that there should be relief against the United States under the FTCA. Cf. *Stencel Aero Engineering Corp.* v. *United States*, 431 U.S. 666, 673 (1977).

CONCLUSION

For these reasons, and those stated in the petition, the petition for a writ of certiorari should be granted and the judgment of the court of appeals should be reversed on the authority of *United States* v. *Neustadt*, 366 U.S. 696 (1961).

REX E. LEE
Solicitor General

MAY 1982

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Petitioner's Brief

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QUESTION PRESENTED

Whether respondent's suit, alleging negligence by a Farmers Home Administration (FmHA) employee in failing during an inspection to discover construction defects in a house respondent purchased from a private builder with a FmHA loan, is excepted from the coverage of the Federal Tort Claims Act as a "claim arising out of * * * misrepresentation" under 28 U.S.C. 2680(h).

PARTIES TO THE PROCEEDING*

Other parties, in addition to those named in the caption, are Charles W. Shuman, Administrator of the Farmers Home Administration; Johnny Vernon Crow, Tennessee State Director of the Farmers Home Administration; S. Lane Parkison, Roane County Supervisor of the Farmers Home Administration; and Mary Wells, Assistant Roane County Supervisor of the Farmers Home Administration.

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* Although respondent's complaint was filed against the Secretary of Agriculture and other Department of Agriculture officials, the United States is the only proper defendant under the Federal Tort Claims Act. See 28 U.S.C. 2674 and 2679(a).

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 4a-18a) is reported at 646 F.2d 1178. The opinion of the district court (Pet. App. 19a-27a) is reported at 489 F. Supp. 512.

JURISDICTION

The judgment of the court of appeals was entered on May 1, 1981 (Pet. App. 2a-3a), and a petition for rehearing was denied on September 28, 1981 (Pet. App. 1a). On December 21, 1981, Justice

O'Connor extended the time in which to file a petition for a writ of certiorari until February 10, 1982. The petition was filed on February 9, 1982, and was granted on May 24, 1982 (J.A. 123). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTES INVOLVED

Section 501(a) of the Housing Act of 1949, 42 U.S.C. (Supp. III) 1471(a), provides in pertinent part:

> The Secretary of Agriculture * * * is authorized, subject to the terms and conditions of this subchapter, to extend financial assistance, through the Farmers Home Administration, (1) to owners of farms in the United States * * * to enable them to construct, improve, alter, repair, or replace dwellings and other farm buildings on their farms, and to purchase buildings and land constituting a minimum adequate site, in order to provide them * * * with decent, safe, and sanitary living conditions and adequate farm buildings as specified in this subchapter, and (2) to owners of other real estate in rural areas for the construction, improvement, alteration, or repair of dwellings, related facilities, and farm buildings and to rural residents for such purposes and for the purchase of buildings and the purchase of land constituting a minimum adequate site, in order to enable them to provide dwellings and related facilities for their own use and buildings adequate for their farming operations * * *.

Section 502(a) of the Housing Act of 1949, 42 U.S.C. 1472(a), provides in pertinent part:

> If the Secretary determines that an applicant is eligible for assistance as provided in section

> 1471 * * * a loan may be made by the Secretary to said applicant for a period of not to exceed thirty-three years * * *.

Section 506(a) of the Housing Act of 1949, 42 U.S.C. 1476(a), provides in pertinent part:

> Buildings and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary. In addition to the financial assistance authorized * * * the Secretary is authorized to furnish * * * technical services such as building plans, specifications, construction supervision and inspection * * *.

Section 509(c) of the Housing Act of 1949, 42 U.S.C. (Supp. IV) 1479(c), provides in pertinent part:

> The Secretary is authorized, after October 1, 1977, with respect to any unit or dwelling newly constructed * * * and purchased with financial assistance authorized by this subchapter which he finds to have structural defects to make expenditures for (1) correcting such defects, (2) paying the claims of the owner of the property arising from such defects, or (3) acquiring title to the property, if such assistance is requested by the owner of the property within thirty-six months after financial assistance under this subchapter is rendered to the owner of the property * * *. Decisions by the Secretary regarding such expenditures or payments under this subsection, and the terms and conditions under which the same are approved or disapproved, shall not be subject to judicial review.

The Federal Tort Claims Act, 28 U.S.C. 2680, provides in pertinent part:

> The provisions of this chapter and section 1346(b) of this title [conferring jurisdiction on the district courts] shall not apply to—
>
> * * * * *
>
> (h) Any claim arising out of assault, battery, false imprisonment, false arrest, malicious prosecution, abuse of process, libel, slander, misrepresentation, deceit, or interference with contract rights * * *.

STATEMENT

1. The Farmers Home Administration (FmHA) is the federal agency authorized by the Secretary of Agriculture, pursuant to Title V of the Housing Act of 1949, 42 U.S.C. (& Supp. IV) 1471 *et seq.*, to extend financial assistance to low-income rural residents to help them acquire "decent, safe, and sanitary living conditions." 42 U.S.C. (Supp. III) 1471(a). FmHA may provide this assistance either by direct loans from the Secretary of Agriculture (42 U.S.C. (& Supp. IV) 1472) or by insured or guaranteed loans (42 U.S.C. (& Supp. IV) 1487).

Regardless of the form of the assistance, FmHA's regulations declare generally that "[s]upervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect the interests of the Government * * *." 7 C.F.R. 1822.7 (a) (1977). Specifically, the regulations in effect at all times relevant to this case provided that (7 C.F.R. 1804.4(g)(3) (1977)):

> The County Supervisor will inspect development work as frequently as necessary to assure that construction and land development conforms with the plans and specifications. He will make a

> final inspection at the earliest possible date after completion of the planned development * * *.[1]

In 1977, Congress amended Section 509(c) of the Housing Act of 1949 to provide administrative relief to FmHA loan recipients whose house is discovered to have "structural defects." 42 U.S.C. (Supp. IV) 1479(c). In that situation the Secretary of Agriculture has unreviewable discretion either to "make expenditures" to correct such defects, to pay the owner for claims arising from such defects or to buy the property. *Ibid.*

2. In 1977, respondent obtained a Rural Housing Loan from FmHA pursuant to Section 502(a) of the

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[1] The Department of Agriculture amended the FmHA regulations effective June 12, 1980. 45 Fed. Reg. 39789. Section 1804.4(g)(3) was deleted and its substance was reenacted as 7 C.F.R. 1924.9(a), with the following addition:

> FmHA's inspections are not to assure the borrower that the house is built in accordance with the plans and specifications. The inspections create or imply no duty or obligation to the particular borrower but are, rather, for the dual purposes of determining that FmHA has adequate security for its loan and enabling FmHA to determine that FmHA is working toward achieving the statutory goal of providing adequate housing.

The Department of Agriculture explained the change as follows:

> [E]xisting statutes provide for these construction inspections to be conducted by FmHA personnel solely to determine adequacy of the FmHA security. Language other than that contained in the final rule may create legal problems by not properly informing the public as to the purpose of these inspections.

45 Fed. Reg. 39792 (1980). Thus, the new regulations were intended to clarify preexisting law on this issue.

Housing Act of 1949, 42 U.S.C. 1472(a) (Pet. App. 5a). Thereafter, respondent contracted with a local builder, Home Marketing Associates, Inc., to construct a prefabricated house (*ibid.*). During the course of construction, Mary Wells, an Assistant County Supervisor for FmHA, as required by FmHA regulations (7 C.F.R. 1804.4(g)(3) (1977)), inspected the house on three occasions and signed the inspection reports.[2] None of the reports contained any adverse comments on the condition of the house or its compliance with FmHA plans and specifications (Pet. App. 6a). Respondent, as well as Ms. Wells, signed the final inspection report (J.A. 66).

Two months later, respondent notified FmHA and the building contractor that the heat pump in her house was malfunctioning. An FmHA inspector went to the house and discovered other construction defects, in addition to the heat pump, that the contractor had left in the house (J.A. 52-53). FmHA notified the contractor of the problem and demanded that it cure the defects, but the contractor refused (Pet. App. 6a). FmHA subsequently granted respondent's administrative request to pay for correcting some, but not all, of the defects pursuant to 42 U.S.C. (Supp. IV) 1479(c) (Pet. App. 7a).[3]

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[2] The inspections were conducted when the house was approximately 2% complete (following completion of the excavation and footings), 99% complete, and 100% complete (J.A. 77, 89).

[3] In addition, we are informed by the FmHA that because of this and other shoddy construction work that Home Marketing Associates, Inc., had performed on FmHA-financed hous for FmHA loan recipients for two years.

3. After the contractor refused to correct the defects that had been identified, respondent filed the instant suit in the Circuit Court of Roane County, Tennessee, against the Secretary, other Department of Agriculture officials who administer the FmHA program, and the private builder who constructed the house. The federal officials removed the case to the United States District Court for the Eastern District of Tennessee pursuant to 28 U.S.C. 1441. After removal, respondent amended her complaint to allege causes of action based on the Tucker Act, 28 U.S.C. 1346(a)(2), and the Federal Tort Claims Act, 28 U.S.C. 2671 *et seq.* (J.A. 3-20). Respondent sought damages of $10,000 for petitioners' breach of contract and negligence in "their supervision and planning [of respondent's] new home and negligently omitt[ing] to perform their supervisory and planning functions" and $10,000 for "pain and anxiety" (J.A. 12).[4]

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[4] Respondent also sought mandamus to compel the Secretary of Agriculture to compensate her, under 42 U.S.C. (Supp. IV) 1479(c), for the construction defects FmHA had identified in her house (Pet. App. 24a-26a). The district court dismissed the mandamus count (*id.* at 26a), and respondent did not challenge that ruling in the court of appeals.

Respondent's original state court complaint did not describe her claim as one arising solely under federal law, and (except for one brief reference to the Federal Tort Claims Act) the claim appears to have been based on state common law. She simply sued the government employees in their official and individual capacities for the costs of repairing the defects that the government had allegedly negligently failed to discover. At the time the case was in state court, therefore, no one understood the suit to be based solely on the Federal Tort Claims Act and thus within the exclusive jurisdiction of the federal courts, 28 U.S.C. 1346(b). Accordingly, we assume that there was some residual basis for the state

The district court dismissed the complaint against the federal defendants for failure to state a claim upon which relief could be granted (Pet. App. 26a) and remanded the suit against the contractor to state court. It reasoned that "[t]o hold the FmHA liable for the shoddy work of the contractor would be tantamount to making a mortgagee the warrantor of the quality of its security" (*id.* at 23a). The court concluded that the FmHA statutes and regulations did not create such a duty running to respondent, and that, to the contrary, the primary purpose of the inspection process was to enable the government to protect its security interest in houses financed under Section 502 (Pet. App. 22a-23a).

The court of appeals reversed (Pet. App. 4a-18a). The court of appeals upheld the district court's determination that the statute and regulations governing the FmHA's inspections did not give rise to a contractual duty to protect respondent from defects in the construction of her home (*id.* at 9a-11a). It rejected, however, the district court's determination that there was no tort liability (*id.* at 11a-18a). Instead, the court of appeals found that the FmHA had

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court's jurisdiction at the time of removal. See *McGowan* v. *Williams*, 623 F.2d 1239 (7th Cir. 1980).

In the district court, after the complaint was amended, it became clear from respondent's brief in opposition to the government's motion to dismiss (C.A. App. 50) that the basis for respondent's suit was the Federal Tort Claims Act, and the district court treated it as such. ("C.A. App." refers to the Appendix filed in the court of appeals.) We thus believe that the district court either had jurisdiction as a result of the removal or that the amended complaint, which was filed within the statute of limitations, effectively initiated the suit in federal court properly under Section 1346(b).

breached the duty created under the common law Good Samaritan doctrine.[5]

The court of appeals reasoned that the government, having voluntarily undertaken to inspect respondent's house, was liable for all injuries caused by the negligent failure to discover any defects in the construction of the house (Pet. App. 11a-13a). The court stated that "Congress, we believe, intended [respondent] to be the beneficiary of the inspection and technical assistance offered by FmHA given the purpose of the Act and the [respondent's] particular circumstances" (*id.* at 17a). In holding that respondent's complaint stated a claim under the Federal Tort Claims Act, the court distinguished *United States* v. *Neustadt*, 366 U.S. 696 (1961), as "a situation dealing with a cause of action based on misrepresentation [rather than] a cause of action based on negligent performance of an operational task" (Pet. App. 16a).

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[5] The court of appeals relied on the *Restatement (Second) of Torts* § 323, at 135 (1965), which provides:

> One who undertakes, gratuitously or for consideration, to render services to another which he should recognize as necessary for the protection of the other's person or things, is subject to liability to the other for physical harm resulting from his failure to exercise reasonable care to perform his undertaking, if
>
> (a) his failure to exercise such care increases the risk of such harm, or
>
> (b) the harm is suffered because of the other's reliance upon the undertaking.

The court of appeals did not, however, discuss whether Tennessee law recognizes these principles, a prerequisite to a finding of liability under the FTCA in any event. See *Feres* v. *United States*, 340 U.S. 135, 141-142 (1950).

SUMMARY OF ARGUMENT

1. The Federal Tort Claims Act, which authorizes suits against the United States for the torts of federal employees, exempts from its waiver of sovereign immunity suits that "aris[e] out of * * * misrepresentation." 28 U.S.C. 2680(h). In this case, the court of appeals held that the misrepresentation exception did not bar a suit alleging negligence by an FmHA employee in failing adequately to inspect the construction of an FmHA-financed house that subsequently proved to have defects. The court reached this decision as a result of its conclusion (Pet. App. 17a) that respondent's claim was "based not on misrepresentation, as in the issuance of a false or inaccurate appraisal report, but rather on [the agency's] failure to use due care in a voluntary undertaking, i.e., inspection and supervision of the construction of her house."

A. The court of appeals' ruling is directly contrary to this Court's decision in *United States* v. *Neustadt*, 366 U.S. 696 (1961). In *Neustadt*, this Court recognized that the misrepresentation exception precludes suits against the United States for damages arising out of the government's failure properly to obtain and communicate information to the plaintiff concerning the condition of a house purchased with federally-provided or guaranteed funds. *Id.* at 706. Here, respondent purchased a home constructed with funds supplied by the Farmers Home Administration after an FmHA inspector had certified that the construction was satisfactory. Thus, despite respondent's attempt to characterize her claim differently, under traditional common law principles (see *Restatement (Second) of Torts* § 311, Illustration 8, at 108-109 (1965) and § 552, Illustration 16,

at 139 (1977)) the gist of respondent's claim is one for misrepresentation, and it is thus barred under 28 U.S.C. 2680(h).

The court of appeals held that this case is controlled not by *Neustadt* but by *Indian Towing Co.* v. *United States*, 350 U.S. 61 (1955), where the government was held liable for failing to maintain a beacon lamp in a lighthouse operated by the Coast Guard. But to state the facts of *Indian Towing* is sufficient to show that it in no way involved a claim for misrepresentation. See *United States* v. *Neustadt*, *supra*, 366 U.S. at 711 n.26. The key difference is that if the FmHA had not been negligent in its inspection of respondent's house, the injury to respondent would still have occurred unless the inspector communicated her findings to respondent. By contrast, in *Indian Towing*, proper maintenance of the lighthouse would have fully protected the plaintiff. This distinction has been recognized by every other court of appeals that has considered the problem.

B. The language and legislative history of the Housing Act of 1949 demonstrate that Congress did not intend the FmHA's inspection activities to transform its rural loan program into a "guaranty or warranty to the purchaser of value received." *United States* v. *Neustadt*, *supra*, 366 U.S. at 709. The primary purpose of the inspection program is to protect the government's security interest. S. Rep. No. 84 (Pt. 2), 81st Cong., 1st Sess. 20 (1949); H.R. Rep. No. 590, 81st Cong., 1st Sess. 12, 56 (1949). In this regard, the 1949 Act is indistinguishable from the 1934 Act at issue in *Neustadt*, which this Court recognized did not suspend the exemption from liability

for misrepresentation in Section 2680(h). 366 U.S. at 708-710.

Respondent nonetheless claims that the FmHA has an obligation, upon discovering defects during the inspection process, not merely to inform the purchaser of the problems but also to withhold the loan from the purchaser until all defects—no matter how minor—have been corrected. Such an interpretation, however, is completely unsupported by both the statute and its implementing regulations. Moreover, respondent's construction of the Housing Act would greatly disrupt the FmHA loan process—a result that Congress could not have intended.

2. The decision below also misconstrues the statutory scheme because it ignores Congress' response to the problem of housing defects that have not been discovered by a FmHA supervisor. Congress has devised an adequate administrative remedy for persons such as respondent, in lieu of allowing them to sue the government under the Federal Tort Claims Act. This program, established in 1977, was intended to replicate an administrative remedy created initially in the wake of *Neustadt* for buyers of FHA-financed homes. The earlier statute was enacted with the express recognition that it would not enlarge rights available to the public under the FTCA. *Payment of Claims for Defects in FHA Homes: Hearings on S. 1200 and S. 2226 Before a Subcomm. of the Senate Comm. on Banking and Currency*, 88th Cong., 1st Sess. 133-134 (1963). Hence, the court of appeals' ruling is inconsistent with Congress' judgment that the exclusive remedy in cases such as this one should be administrative, rather than judicial.

ARGUMENT

A SUIT ALLEGING A NEGLIGENT FAILURE BY A FARMERS HOME ADMINISTRATION EMPLOYEE ADEQUATELY TO INSPECT THE CONSTRUCTION OF A HOUSE THAT IS SUBSEQUENTLY DISCOVERED TO HAVE DEFECTS IS BARRED BY THE "MISREPRESENTATION" EXCEPTION TO SUITS ALLOWED AGAINST THE UNITED STATES UNDER THE FEDERAL TORT CLAIMS ACT, 28 U.S.C. 2680(h)

In 1946, Congress adopted the Federal Tort Claims Act, which makes the United States generally liable to the same extent as a private party for injuries caused by the negligent acts of federal employees. 28 U.S.C. 1346(b). Although Congress concluded that it was prudent to waive the sovereign immunity of the United States for many "ordinary common-law torts," *Dalehite* v. *United States*, 346 U.S. 15, 28 (1953), it also recognized that there are "a series of torts as to which, for the time being at least, it may be dangerous for the government to subject itself to suit * * *." *Hearings Before a Subcomm. of the House Comm. on the Judiciary*, 76th Cong., 3d Sess. 13 (1940); *id.* at 22. See also S. Rep. No. 1400, 79th Cong., 2d Sess. 33 (1946); H.R. Rep. No. 1287, 79th Cong., 1st Sess. 6 (1946). Thus, when Congress enacted the Tort Claims Act, it expressly exempted the United States from "[a]ny claim arising out of," *inter alia*, "misrepresentation." 28 U.S.C. 2680(h). Under the "accepted jurisprudential principle that no action lies against the United States unless the legislature has authorized it," *Dalehite* v. *United States*, *supra*, 346 U.S. at 30; see also *United States* v. *Orleans*, 425 U.S. 807, 814 (1976); *Feres* v. *United States*, 340 U.S. 135, 139 (1950); *United States* v. *Shaw*, 309 U.S. 495, 504 (1940); *United States* v.

Eckford, 73 U.S. (6 Wall.) 484, 488 (1867), if respondent's suit—alleging negligent inspection and supervision in the construction of her house—is one "arising out of * * * misrepresentation," then recovery against the United States is barred.

A. Respondent's Claim "Arises Out Of" Misrepresentation Within The Meaning Of 28 U.S.C. 2680(h), As Interpreted By This Court In *United States* v. *Neustadt*

1. This Court previously interpreted the misrepresentation exception to the Tort Claims Act in *United States* v. *Neustadt*, 366 U.S. 696 (1961). In *Neustadt*, the owners of a house had obtained a Federal Housing Administration (FHA) appraisal and secured a mortgage insurance commitment (based on the appraisal) in order to facilitate the sale of the house. After plaintiffs purchased the house from the owners, major foundation defects were discovered that substantially decreased its market value.

Plaintiffs then filed suit under the Federal Tort Claims Act for the difference between the fair market value of the house and the price for which they had purchased it, alleging that the FHA's inspection had been negligently conducted, and that, if it had been performed properly, they would never have purchased the house. The Fourth Circuit affirmed the judgment in plaintiffs' favor, reasoning that since the government owed a statutory duty to plaintiffs to furnish them with a written appraisal prior to sale, it was liable if it performed its appraisal duty negligently, "even though the careless performance of the duty may have been accompanied by some misrepresentation of fact." *United States* v. *Neustadt*, 281 F.2d 596, 599 (4th Cir. 1960).

Finding that plaintiffs' complaint arose out of misrepresentation, rather than negligence, this Court reversed. The Court squarely rejected the argument that Section 2680(h) does not apply "when the gist of the claim lies in *negligence* underlying the inaccurate representation, *i.e.*, when the claim is phrased as one 'arising out of' negligence rather than 'misrepresentation'." 366 U.S. at 703 (emphasis in original). Thus, the Court in *Neustadt* recognized that the exceptions in Section 2680(h) are not mere rules of pleading; the United States cannot be held liable under the Tort Claims Act simply by a plaintiff's steadfast refusal to include the magic word "misrepresentation" in his complaint. See also *Fitch* v. *United States*, 513 F.2d 1013, 1015 (6th Cir. 1975); *Hall* v. *United States*, 274 F.2d 69, 71 (10th Cir. 1959); Note, *Federal Tort Claims Act—Exceptions—Intentional Torts*, 7 Vand. L. Rev. 283, 284 (1954).

Instead, the Court required an examination of the basic nature of the plaintiff's allegations to determine whether, fairly interpreted, they state a cause of action for misrepresentation as that term was understood at common law when the Tort Claims Act was adopted. The Court explained (366 U.S. at 706-707):

> To say, as the Fourth Circuit did, that a claim arises out of "negligence," rather than "misrepresentation," when the loss suffered by the injured party is caused by the breach of a "specific duty" owed by the Government to him, *i.e.*, the duty to use due care in obtaining and communicating information upon which that party may reasonably be expected to rely in the conduct of his economic affairs, is only to state the traditional and commonly understood legal definition of the tort of "negligent misrepresentation" * * *

> which there is every reason to believe Congress had in mind when it placed the word "misrepresentation" * * * in § 2680(h).[6]

Respondent's claim is in all material respects identical to that of the Neustadts (see note 10, *infra*). Applying the teaching of *Neustadt* to this case, the claim clearly is one "arising out of" misrepresentation.

As the authorities cited by the Court in *Neustadt* uniformly recognize, a cause of action for negligent misrepresentation arises out of a defendant's failure to exercise due care in *obtaining* information and/or in communicating it.[7] *Restatement of Torts* § 552 (1938); W. Prosser, *Torts* § 87 (1941). See *United*

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[6] In adopting this construction of "misrepresentation," the Court merely followed the established rule that Congress is presumed to have intended to incorporate the "judicially settled meaning" or application of a term. See *United States* v. *Merriam*, 263 U.S. 179, 187 (1923); *Kepner* v. *United States*, 195 U.S. 100, 124 (1904); *The "Abbotsford,"* 98 U.S. 440, 444 (1878). Respondent does not appear to challenge the basic interpretation of "misrepresentation" adopted by the Court in *Neustadt*.

[7] Given the history of the tort of negligent misrepresentation, it is not surprising that Congress would decline to allow recovery for it under the Tort Claims Act. England denied recovery for all negligent misrepresentations until 1963. Compare *Derry* v. *Peek*, 14 App. Cas. 337 (1889), with *Hedley Byrne & Co.* v. *Heller & Partners*, [1964] App. Cas. 465. According to Dean Prosser, a majority of courts in this country follow *Derry* v. *Peek* and deny recovery for innocent or negligent misrepresentations. The fear generally is that the scope of liability would be difficult to limit once recovery is recognized. See W. Prosser, *Handbook of the Law of Torts* 706-707 (4th ed. 1971); *Ultramares Corp.* v. *Touche*, 255 N.Y. 170, 179, 174 N.E. 441, 444 (1931). Obviously, the tort of misrepresentation carries with it a substantial basis for concern regarding the scope of liability to which the United States might be subjected (see page 13, *supra*).

States v. *Neustadt*, *supra*, 366 U.S. at 706-707 n.16. See generally Bohlen, *Misrepresentation as Deceit, Negligence, or Warranty*, 42 Harv. L. Rev. 733 (1929); Bohlen, *Should Negligent Misrepresentations Be Treated as Negligence or Fraud?*, 18 Va. L. Rev. 703 (1932). Here, FmHA allegedly was negligent in failing to identify certain defects in the construction of respondent's house and therefore in failing to note those defects in the inspection forms it executed, including the one respondent signed. Based on FmHA's certification that the construction was satisfactory, the loan money was released to respondent and she proceeded to purchase the house from the contractor. Thus, as in *Neustadt*, any damages suffered by respondent occurred solely as a result of the FmHA inspector's "representation" that the house was without defects, not because of the government's inspection.[8]

The *Restatement (Second) of Torts* § 552, Illustration 18, at 139 (1977), offers the following illustration as the archetypal case of negligent misrepresentation:

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[8] An illustration accompanying Section 552's companion provision (defining negligent misrepresentation that results in personal injury as well as property damage) describes a situation directly analogous to the instant case, and virtually identical to that presented in *Reynolds* v. *United States*, 643 F.2d 707 (10th Cir.), cert. denied, No. 80-2064 (Oct. 5, 1981):

> The A Boiler Insurance Company undertakes as part of its services to inspect the boiler of B. It issues a certificate that the boiler is in good condition for use. In reliance upon this certificate, B uses the boiler. The boiler bursts, owing to a defect which a reasonably careful inspection would have disclosed. Explosion of the boiler wrecks the adjacent building of C and causes bodily harm to him. The A Company is subject to liability to C for his bodily harm and the wrecking of his building caused by the explosion of the boiler.

Restatement (Second) of Torts § 311, Illustration 8, at 108-109 (1965).

> A, a United States government food inspector, in the performance of his official duties, negligently stamps a quantity of B's beef as "Grade A." In fact the beef is of inferior quality. In reliance upon the stamps, C buys the beef from D, and suffers pecuniary loss as a result. A is subject to liability to C.

By simply modifying the hypothetical slightly to refer to a government housing inspector, the facts of this case become identical to those in the illustration.[9] See also *Anglo-American & Overseas Corp.* v. *United States*, 144 F. Supp. 635, 636 (S.D.N.Y. 1956), aff'd, 242 F.2d 236 (2d Cir. 1957). Hence, it is clear that respondent's claim is one that "arises out of" misrepresentation as that term was understood at common law.

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[9] Prior to the enactment of the Tort Claims Act, it was common for inspectors to be sued under a theory of negligent misrepresentation for the "careless performance of a service" leading to "careless words" certifying the existence of a particular set of facts. *Glanzer* v. *Shepard*, 233 N.Y. 236, 135 N.E. 275 (1922). See also *Mulroy* v. *Wright*, 185 Minn. 84, 240 N.W. 116 (1931); *Ultramares Corp.* v. *Touche*, 255 N.Y. 170, 174 N.E. 441 (1931); *National Iron & Steel Co.* v. *Hunt*, 312 Ill. 245, 143 N.E. 833 (1924); *Gordon* v. *Livingston*, 12 Mo. App. 267 (1882); *Tardos* v. *Bozant*, 1 La. Ann. 199 (1846); Annot., 68 A.L.R. 375 (1930); Annot., 34 A.L.R. 63 (1925); F. Harper, *A Treatise on the Law of Torts* § 76 (1933). In some cases, however, recovery was denied because the particular state did not recognize the tort of negligent misrepresentation.

As this Court observed in *Neustadt*, it is reasonable to assume that when Congress used the term "misrepresentation" in Section 2680(h) it intended the term to incorporate its common law applications, which plainly included liability for negligent inspections and certifications. See note 6, *supra*. Moreover, it is significant that Congress exempted the United States not merely from claims of misrepresentation, but for all claims, however couched, "arising out of" misrepresentation.

Indeed, if respondent's suit were not brought pursuant to the Tort Claims Act, her claim surely would be styled as one for misrepresentation. Because the Tort Claims Act does not waive the sovereign immunity of the United States from damages caused by the misrepresentations of its employees, plaintiffs such as respondent are forced to avoid such allegations. Thus, respondent (Br. in Opp. 28) has asserted that her suit is really one for negligent failure to withhold loan money. Similarly, the Neustadts had argued that their claim was really one for "negligence * * * in the issuance of mortgage insurance." [10] But

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[10] The Neustadts had asserted (Br. for Resp. at 26-27, *United States* v. *Neustadt*, No. 533, 1960 Term):

> The Government has failed to focus clearly upon the chain of events which led to the injury suffered by respondents. Respondents are not complaining of the fact that they were told something that was not true and that in reliance thereon they took action to their detriment. In point of fact, the appraisal report which they received was not given them until the time of the closing of the purchase transaction. By the terms of their contract of sale they were obligated to accept a deed to the property provided only that FHA mortgage insurance was available. It was the availability of this insurance and not the receipt of the appraisal report that caused them to purchase the defective house. Had that mortgage insurance not been issued the respondents could not and would not have purchased the house. They are complaining, then, that the inspector's negligence in the performance of his function of making an inspection of the premises—a function that the Congress has unequivocally stated was intended to offer protection to the prospective home buyer—resulted in the issuance of mortgage insurance and consequently in respondents' purchase of a defective structure.

Respondent makes a strikingly similar contention here (Br. in Opp. 28):

in rejecting this contention, this Court in *Neustadt* clearly held that a claim for failure to withhold a loan or to withhold mortgage insurance because an inspection failed to discover a defect is a claim "arising out of" misrepresentation, which Congress refused to permit as a basis for suit against the United States. This holding, which Congress in the past 20 years has declined to disturb, controls this case.

2. In an attempt to avoid the clear mandate of *Neustadt*, the court of appeals asserted (Pet. App. 13a) that its decision was controlled instead by *Indian Towing Co.* v. *United States*, 350 U.S. 61 (1955), a decision the Court in *Neustadt* was careful to preserve. See 366 U.S. at 711 n.26. *Indian Towing Co.* involved the Coast Guard's failure properly to maintain the beacon lamp in a lighthouse, which caused a vessel to run aground. As the Court in *Neustadt* noted, "[s]uch a claim does not 'arise out of * * * misrepresentation' * * *." 366 U.S. at 711 n.26.

FmHA asserts that the gravamen of Miss Neal's complaint is that "the government was negligent in not discovering the defects and disclosing their existence to her." (Pet. p. 10). This characterization of her claim is incorrect and ignores the record below and the specific findings by the court of appeals. Her complaint is not based on failure to disclose or misrepresentation. The facts and allegations in the complaint show that FmHA undertook inspection and supervision of the construction of Miss Neal's home. If FmHA's inspection had been done properly and with due care, *FmHA* could have prevented injury to her by withholding funds from the contractor until the defects were corrected.

To achieve the purpose of supervision and inspection FmHA need not make a representation of any kind to Miss Neal or any other borrower and Miss Neal has not claimed that a misrepresentation was made.

This case, however, is identical to *Neustadt*, and the distinction the Court recognized between *Neustadt* and *Indian Towing Co.* is the reason respondent's suit should be barred. In *Indian Towing Co.*, if the Coast Guard had maintained the lighthouse properly, that would have completely protected the plaintiff, and no additional act of communication would have been required. Here, by contrast, even if the FmHA had not been negligent in its inspection and had discovered the defects in the house, respondent's injury would still have occurred unless that information was conveyed to her.[11] Thus, the basis for respondent's claim ultimately rests on a failure of the inspection document to disclose the existence of those defects. The inspector's approval was a representation to respondent that the house was without defects, and the injury she suffered was caused by that misrepresentation, not by the government's negligent inspection.

Prior to the Sixth Circuit's decision in this case, the courts of appeals had carefully distinguished between the *Indian Towing Co.* situation, where government operations directly cause an injury, and the *Neustadt* situation, where the injury is caused by the government's failure to obtain and supply accurate information. Compare, *e.g.*, *Baroni* v. *United States*, 662 F.2d 287 (5th Cir. 1981), petition for cert. pending, No. 81-1326 (filed Jan. 12, 1982); *Reynolds* v. *United States*, 643 F.2d 707 (10th Cir.), cert. denied, No. 80-2064 (Oct. 5, 1981); *City of San Francisco* v. *United States*, 615 F.2d 498 (9th Cir. 1980);

[11] This basic point is emphasized by the fact that the FmHA merely released the loan proceeds to *respondent* in her supervised account (see note 18, *infra*) following its inspections. Respondent's injury occurred not at that point but when *she* paid the money to the contractor, allegedly on the basis of the FmHA's misrepresentation that the house was free of defects.

Preston v. *United States*, 596 F.2d 232 (7th Cir.), cert. denied, 444 U.S. 915 (1979); *Somali Development Bank* v. *United States*, 508 F.2d 817, 821 (Ct. Cl. 1974); *Thompson* v. *United States*, 408 F.2d 1075, 1081 (8th Cir. 1969); *Cenna* v. *United States*, 402 F.2d 168 (3d Cir. 1968); *National Manufacturing Co.* v. *United States*, 210 F.2d 263, 276 (8th Cir.), cert. denied, 347 U.S. 967 (1954); *Anglo-American & Overseas Corp.* v. *United States*, 144 F. Supp. 635, 636 (S.D.N.Y. 1956), aff'd, 242 F.2d 236 (2d Cir. 1957), with *Ware* v. *United States*, 626 F.2d 1278 (5th Cir. 1980); and *Hall* v. *United States*, 274 F.2d 69 (10th Cir. 1959). The court below failed to recognize this clear distinction by focusing only on respondent's generalized claim of negligence as the basis for the suit, thus ignoring the plain fact that respondent's injury (like the injury in *Neustadt*) "arises out of" a negligent *misrepresentation*.

B. The Housing Act Of 1949 Creates No Cause Of Action Against The United States That Is Not Barred By The "Misrepresentation" Exception To The Federal Tort Claims Act

1. Although its reasoning is somewhat cloudy, the court of appeals seems to have held (Pet. App. 17a) that Section 506 of the Housing Act of 1949, 42 U.S.C. (& Supp. IV) 1476, was "intended, in a case such as this, to limit or suspend the application of the 'misrepresentation' exception of the Tort Claims Act." *United States* v. *Neustadt*, *supra*, 366 U.S. at 708. This Court rejected this precise argument in *Neustadt* with regard to the inspection and appraisal provisions in the National Housing Act of 1934, 12 U.S.C. 1709 and 1715q. Respondent contends, however, that the statute in this case is very different from that in *Neustadt*.

We agree that Sections 203 and 226 of the National Housing Act of 1934, 12 U.S.C. 1709 and

1715q, at issue in *Neustadt*, and Section 506 of the Housing Act of 1949, 42 U.S.C. (& Supp. IV) 1476, involved in this case, differ in certain respects. The nature of the statutes, however, as well as their implementing administrative schemes and common sense, compel the conclusion that the differences that exist are immaterial for purposes of the government's liability under the Federal Tort Claims Act.

Section 501 of the Housing Act of 1949 authorizes the Secretary of Agriculture to extend financial assistance to low-income rural residents to help them acquire "decent, safe, and sanitary living conditions." 42 U.S.C. (Supp. III) 1471(a). Section 506(a) of the Act, however, on which respondent primarily relies, merely authorizes the Secretary to create a program for inspecting houses constructed with FmHA funds. 42 U.S.C. 1476(a). Nothing in that provision specifies that the *inspection program* is, or should be, for the benefit of the loan recipient. On the contrary, the legislative history of the 1949 Act clearly indicates that the purpose of requiring inspection and supervision is precisely the same as that underlying the appraisal report provisions involved in *Neustadt* —the protection of the government's interest in the loans it makes.[12] The Senate Report accompanying Title V of the 1949 Act states that "[t]he extent of the requirements for building plans, supervision, and inspection would depend upon the character of the construction and the *amount of the loan*." S. Rep. No. 84 (Pt. 2), 81st Cong., 1st Sess. 20 (1949) (em-

[12] In *Neustadt*, the FHA only guaranteed the loan, whereas here the FmHA actually provided the money for the loan. But in both cases the government's primary concern with regard to inspections was to ensure that its resources were protected. The interests of a lender are no different from those of a guarantor with respect to construction defects that do not undermine the security interest.

phasis added). See also H.R. Rep. No. 590, 81st Cong., 1st Sess. 12, 56 (1949); 95 Cong. Rec. 4764 (1949) (remarks of Sen. Langer). An inspection that is dependent on the size of the loan involved obviously is not intended primarily to benefit the home buyer, but instead is designed to protect the lender's financial investment. The FmHA has recognized this purpose in regulations that have been in effect since 1966, 31 Fed. Reg. 14113, and which state explicitly that "supervision" is provided in order "to protect the interests of the Government * * *." 7 C.F.R. 1822.7(a) (1977).[18] This long-standing interpretation by the agency responsible for

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[18] Respondent attempts (Br. in Opp. 18) to convert a general statement in the regulations (7 C.F.R. 1802.2 (1977)) about the overall purpose of "supervision" into a specific guarantee of "decent, safe, and sanitary housing" to be accomplished through the inspection process. But inspection is not a large part of the supervisor's job (J.A. 71-72, 107) and appears not to be at all relevant to the supervisor's effort to provide decent housing. In the regulation describing the County Supervisor's responsibilities for supervision of the home buyer, there is no mention of inspections for defects. Instead, the regulation provides for "[t]imely guidance by letter or other means of communications" (7 C.F.R. 1802.3(g) (1977)).

Moreover, regulations in effect at the time respondent applied for her FmHA loan, which were incorporated by reference in the promissory note and deed of trust she executed (J.A. 32-46), were intended to discourage loan recipients from relying on the inspection process as a guarantee by FmHA that all construction requirements had been met. See 7 C.F.R. 1804.4(d)(6)(i)(a) (1977) ("[A]lthough the FmHA is interested in the proper execution of the contract, it will not become a party to the contract nor incur any liability thereunder"). The regulation in effect today (see note 1, *supra*) is even more explicit, further clarifying what was already quite clear—that the inspections create no basis for liability.

the day-to-day administration of the Act is entitled to great deference. See *Udall* v. *Tallman*, 380 U.S. 1, 16 (1965).

In fact, the purpose and structure of the Housing Act of 1949 are in many respects similar to those of the statute involved in *Neustadt*. The National Housing Act of 1934 was styled "[a]n act to encourage improvement in housing standards and conditions" (Act of June 27, 1934, ch. 847, 48 Stat. 1246), thus indicating the same general purpose to assist home buyers as in the 1949 Act. Moreover, the 1934 Act's legislative history clearly indicates that its inspection/appraisal provision was intended to benefit the home buyer. The Conference Report, for example, states: "[T]hese FHA [inspection and appraisal] procedures also operate for the benefit and protection of the individual home buyer." H.R. Conf. Rep. No. 2271, 83d Cong., 2d Sess. 66 (1954). Despite this general purpose, this Court recognized in *Neustadt* that the 1934 statute was not intended to create a basis for governmental liability when an FHA inspector failed to discover a defect in a house or, if discovered, failed to take some action to correct it. 366 U.S. at 709-710.[14]

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[14] While *Neustadt* suggests that an inspection program by its nature may give rise to an obligation to disclose whatever defects are discovered, it also establishes that the breach of such a duty is not actionable under the Tort Claims Act because of the misrepresentation exception. 366 U.S. at 700-708. And while the Court's opinion indicates that an inspection program could give rise to a statutorily created duty to warrant the quality of the construction, the decision also makes it plain that Congress must clearly have intended such a result. *Id.* at 708. Here, we submit, there is no basis for concluding that "Congress intended, in a case such as this, to limit or suspend the application of the 'misrepresentation' exception of the Tort Claims Act." *Ibid.*

Respondent contends (Br. in Opp. 28), however, that her claim is based not on the government's failure to discover and disclose the construction defects for which she seeks damages, but instead on FmHA's failure to discover such defects and thereafter to withhold payment *from her* until all identified problems had been corrected.[15] Besides the fact that these allegations appear designed solely to avoid making a traditional misrepresentation claim (see page 19, *supra*), respondent's contention requires an interpretation of the FmHA's obligations under the Housing Act of 1949 and its implementing regulations that simply defies common sense. On the basis of three relatively brief inspections of between 10 and 30 minutes (J.A. 77, 89) and the provision of a loan designed to assist low-income rural residents to acquire decent housing, respondent would create an obligation on the FmHA not only to detect all defects in her house, but also to refuse to release loan money needed by her to purchase the house from the builder until every defect is corrected. For this novel suggestion respondent relies (Br. in Opp. 28) exclusively on the deposition of a contractor, who merely stated that it was his understanding that such action could be taken (J.A. 97). Even this one bare piece of evi-

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[15] Respondent also attempts to avoid the application of the misrepresentation exception by claiming (Br. in Opp. 28) that she did not actually rely upon the inspection report. She did, however, sign the final report at the time of the last inspection and presumably understood it as an approval of the house as constructed. Moreover if her claim does not include an allegation of reliance on the government's failure to discover and disclose any defects, then she has no cause of action at all. See *Baroni* v. *United States*, 662 F.2d 287, 289 (5th Cir. 1981), petition for cert. pending, No. 81-1326 (filed Jan. 12, 1982).

dence is inapposite: the statement in context refers specifically to the situation where the builder seeks to obtain money while the construction is on-going and thus while it is still possible that the government's security interest may not be adequately protected.

As the depositions of the FmHA employees in this case demonstrate, such drastic action would be taken only if the defect were "really important" (Br. in Opp. 26; J.A. 114). The FmHA inspector testified that, for most deviations from specifications that are discovered at the inspection, "[n]ormally we ask [the home buyer], did you want this done, did you agree with this, and if it doesn't depreciate or decrease our security, we go on." (J.A. 113). In addition, the form used by FmHA to record the results of its inspections requires the inspectors to itemize only those "*significant* conditions observed to be at variance with the approved plans and specifications" (J.A. 56) (emphasis added). This evidence regarding the administrative practice comports with the legislative purpose of the inspection scheme to protect the loan, because major defects are most likely to impair the government's security interest.

A scheme such as respondent proposes would impose a burden on the FmHA that would seriously delay all conveyances under the FmHA rural loan program.[16] In addition, under respondent's theory the

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[16] The nature of the defects about which respondent complains graphically demonstrates the enormity of the burden she would impose upon FmHA through its inspection process. Among the problems for which respondent would hold the government liable under the Tort Claims Act are such relatively minor items as the building material used for the porch, the design of the rear service door, the arrangement of the bath, the adequacy of caulking and the quality of the paint

United States would face a massive potential monetary liability, because FmHA closes nearly 90,000 loans per year[17] and virtually all new houses have some defects in them. See J.A. 104. The FmHA repeatedly would face the choice of either withholding loan money at closing until all such problems are corrected or inviting a law suit. Congress could not have intended these consequences. In the case of nonstructural defects that do not jeopardize the government's security interest, the most that can be expected is that the FmHA generally will inform both the builder and the buyer of the problems it discovers during its inspection (J.A. 113).[18] Failure to notify,

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(Br. in Opp. 8; J.A. 52-53). It is unreasonable to assume that Congress expected FmHA inspectors to discover these types of defects in every FmHA-financed house and to assume responsibility for having all of them corrected prior to releasing FmHA loan funds.

[17] Respondent's theory, if adopted, could not easily be limited to FmHA inspections. The federal government engages in inspections and certifications in many analogous circumstances, where the purpose, indirectly or directly, is to benefit some segment of the public. Many of these programs were developed, at least in part, in reliance on this Court's construction of the Tort Claims Act in *Neustadt*. Since Congress in the 20 years since *Neustadt* has not seen fit to subject the United States to the dangers inherent in suits involving misrepresentations, as defined in *Neustadt*, it would be unwarranted for this Court to limit its interpretation of Section 2680(h) as proposed by respondent. See *United States* v. *Mason*, 412 U.S. 391, 399-400 (1273).

[18] The fact that respondent is poor and not well educated is no basis for assuming, in the absence of express congressional indication, that she is free, based on the inspection, to rely solely upon the FmHA to guarantee the quality of her property. Loan recipients are encouraged to participate in the inspections. See 7 C.F.R. 1804.4(g)(1), (g)(3)(ii) and

however, is precisely what this Court in *Neustadt* held was within the misrepresentation exception to the FTCA. In short, nothing in the legislative history of the 1949 Act or in FmHA's administrative regulations provides any basis for distinguishing this program from the 1934 Act that was at issue in *Neustadt*.[19]

(g) (3) (iv) (1977). FmHA Assistant Supervisor Wells testified that respondent accompanied her on at least one of the inspection trips (the last) and possibly another one as well (J.A. 84). Respondent also signed the last inspection report (J.A. 65).

Moreover, it is plain that the primary guarantor of the quality of the building is to be the contractor. The regulations make this clear by requiring the builder to issue a one-year warranty on the construction of the house (7 C.F.R. 1804.4 (d) (1977)), which the builder did here (J.A. 47-51). Indeed, the builder in this case, in response to a question by respondent's counsel, denied that FmHA supervises the construction of FmHA-financed houses (J.A. 105).

Respondent's reliance (Br. in Opp. 27 n.19) on the fact that her account was "supervised" and therefore required co-signing by the County Supervisor as evidence of the FmHA's control over the payment of money pending correction of defects is also misplaced. First, most FmHA loans are supervised because most loan recipients, like respondent, are not experienced in handling large sums of money (J.A. 112). Second, the supervision is designed to assure that the money is not misused by the loan recipient, not to serve as a basis for holding up payments to the builder pending correction of all defects.

[19] In support of her interpretation of the statute, respondent relies (Br. in Opp. 27 n.19) upon 7 C.F.R. 1803.8 (d) (3) (i) (1978), which provides that checks drawn on supervised accounts will be countersigned by an FmHA official "only if the quantity and quality of items purchased are in accordance with approved plans." That provision, however (which, it should be noted, was not in effect when respondent obtained

2. The court of appeals' conclusion that the 1949 Act was intended to limit the misrepresentation exception to the Tort Claims Act completely ignores the congressional scheme for remedying administratively the injury about which respondent complains. Obviously, the first source of protection against the construction of defective housing must be the private developer or builder. See 7 C.F.R. 1924.252.[20] (Indeed, respondent still has pending in state court a suit against the builder, Home Marketing Associates, Inc., in which she has requested relief identical to that she is seeking from the United States in the instant suit.) Congress realized, however, that not all builders will be able or willing to correct or compensate for their faulty construction. Rather than permitting injured home buyers to suffer a severe loss, or amending the Tort Claims Act to allow buyers to sue the federal government for injuries caused in part by the failure to discover and disclose defects during an inspection, Congress chose to provide a discretionary administrative remedy. Thus, in 42 U.S.C. (Supp. IV) 1479(c), Congress authorized the Secretary of Agriculture to grant relief to an FmHA loan

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her loan), deals with the unusual situation where the loan recipient decides to purchase the materials and merely have the contractor come in and work with them. The regulation expressly anticipates that the FmHA will not authorize release of the money to pay for the materials unless the materials are approved by the County Supervisor. The regulation has no application to the situation in this case.

[20] One of the FmHA employees who was deposed in this case made this clear when he informed respondent's counsel that the reason respondent's request for administrative relief had not been processed was because she had not yet exhausted her attempts to obtain relief from the builder (Deposition of S. Lane Parkinson at 95).

recipient whose house has "structural defects" not discovered in the Section 506 inspection process. In such a case, the Secretary may correct the defects, pay for the cost to the buyer of correcting the defects, or purchase the house outright. 42 U.S.C. (Supp. IV) 1479(c); 7 C.F.R. 1924.252.[21]

Section 1479(c) was enacted by Congress in 1977 to give the Secretary of Agriculture essentially the same authority possessed by the Secretary of Housing and Urban Development (see 12 U.S.C. 1735b (b)) with respect to individuals who had purchased defective houses with FHA-insured loans. H.R. Rep. No. 95-236, 95th Cong., 1st Sess. 171-172 (1977). HUD's authority was first granted in 1964, just three years after *Neustadt*, when Congress decided to assist "distressed homeowners who, after relying upon FHA construction standards and inspections, find structural or other major defects in their properties purchased with FHA-insured loans." S. Rep. No. 1265, 88th Cong., 2d Sess. 5 (1964).

At the time Congress took this remedial action, it was well aware of the *Neustadt* decision. In the hearings on the general problem of how to assist these homeowners, *Neustadt* was carefully discussed. Indeed, the General Counsel of the Housing and Home Finance Agency explained in a statement to the Senate Subcommittee that passage of the administrative

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[21] Respondent was granted some relief pursuant to this program, but apparently not all that she requested (Br. in Opp. 11). The Secretary's decision to withhold administrative relief is not judicially reviewable. 42 U.S.C. (Supp. IV) 1479(c).

The Department of Agriculture has informed us that it approved claims under this Section in 332 cases in 1980 and 292 cases in 1981, at a total cost of $589,568 and $720,887, respectively.

remedy to correct structural defects would result in "no modification of the principles relied on in the *Neustadt* case" and would cause "no enlargement of rights under the Federal Tort Claims Act." *Payment of Claims for Defects in FHA Homes: Hearings on S. 1200 and S. 2226 Before a Subcomm. of the Senate Comm. on Banking and Currency*, 88th Cong., 1st Sess. 133-134 (1963). Thus, Congress enacted an administrative remedy in the wake of the *Neustadt* decision, and it deliberately chose to make this the exclusive remedy in *Neustadt*-type cases. See *Summers* v. *United States*, 510 F.2d 123, 125 (8th Cir.), cert. denied, 423 U.S. 851 (1975). See also *Potnick* v. *United States*, 356 F. Supp. 395, 398 (N.D. Miss. 1973) (discussing 38 U.S.C. 1827, a comparable provision for VA-financed housing). In light of Congress' determination to provide discretionary administrative relief for persons such as respondent, rather than to amend the Federal Tort Claims Act, the court of appeals' modification of the clear rule in *Neustadt* is particularly indefensible. See *Laird* v. *Nelms*, 406 U.S. 797, 802 (1972) ("To permit respondent to proceed * * * here would be to judicially admit at the back door that which has been legislatively turned away at the front door. We do not believe the [Federal Tort Claims] Act permits such a result").

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

JOHN R. BLOCK, Secretary of Agriculture, *et al.*,
Petitioners,

v.

ONILEA NEAL, *Respondent.*

On Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

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QUESTION PRESENTED

Whether Onilea Neal's complaint states a claim for relief against the Farmers Home Administration for negligent inspection and supervision of the construction of her home built under a loan from the Farmers Home Administration made pursuant to Title V of the 1949 Housing Act?

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IN THE

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OCTOBER TERM, 1982

No. 81-1494

JOHN R. BLOCK, Secretary of Agriculture, *et al.*,
Petitioners,

v.

ONILEA NEAL, *Respondent.*

On Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

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BRIEF FOR THE RESPONDENT

STATEMENT

Onilea Neal is a 54 year old woman who lives alone in Roane County, Tennessee. Her yearly income from employment as a cafeteria worker at a local elementary school is approximately $3500. She has never been married and has an eleventh grade education. Miss Neal has never previously owned a home. (C.A.App. 139) In 1976, Miss Neal was living in a seriously dilapidated rental dwelling that was scheduled to be torn down by the owner. (J.A. 115-116) She began to look for another place to live, but was unable to find safe and decent housing to rent within her financial means. She was also unable to purchase a house through conventional financing. Finally, she applied for a Section 502 rural housing loan with Farmers

Home Administration ("FmHA") on August 16, 1976.[1] (C.A.App. 139-140)

FmHA is an agency of the United States Department of Agriculture. It administers Title V of the 1949 Housing Act, as amended, which has a stated national goal to provide "a decent home and a suitable living environment for every American family." 42 U.S.C. § 1441. Under Title V, Congress established several loan and technical service programs for rural low-income residents. The relevant provisions of the 1949 Housing Act authorize the Secretary of Agriculture to extend financial and technical assistance, through FmHA, to eligible rural residents in order to provide them "decent, safe and sanitary living conditions." 42 U.S.C. § 1471(a). Financial assistance, in the form of loans for single family owner resident homes, is authorized under § 502 of the 1949 Housing Act, 42 U.S.C. § 1472. Technical assistance is authorized under § 506, 42 U.S.C. § 1476 (emphasis added):

> (a) In connection with financial assistance authorized in this subchapter, the Secretary shall require that all new buildings and repairs financed under this subchapter shall be substantially constructed and in accordance with such building plans and specifications as may be required by the Secretary. Buildings and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary. *In addition* to the financial assistance authorized in this subchapter, the *Secretary is authorized to furnish*, through such agencies as he may determine, *to any person, including a person eligible for financial assistance under this subchapter*, without charge or at such charges as the Secretary may determine, *technical services such as building plans, specifications, construction supervision and inspection,*

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[1] To be eligible for a Section 502 rural housing loan, Onilea Neal had to establish that she was unable to obtain credit from any other source on terms she could reasonably be expected to meet. She had to be without adequate housing and without resources to obtain necessary housing on her own account. 42 U.S.C. § 1471(c).

> and advice and information regarding farm dwellings and other buildings.

The Section 502 rural housing loan program differs from other government housing programs because of FmHA's direct involvement in all operations of the program. In other government home ownership programs, the government plays an important but secondary role to the private lender with whom the borrower has exclusive dealings. In the Section 502 rural housing loan program the borrower deals only with a government employee, known as the county supervisor.[2]

The county supervisor determines eligibility for a Section 502 loan. 7 C.F.R. § 1822.11(b) (1977).[3] He checks a borrower's credit information. 7 C.F.R. § 1822.11(a)(2) (1977). Before a borrower purchases a home site

> The County Supervisor should . . . advise him [borrower] with respect to the size, design, quality, cost and location of the dwellings and dwelling sites suitable for the [Section 502 rural housing] program.

7 C.F.R. § 1822.11(d) (1977). The county supervisor reviews the borrower's proposed plans and specifications for compliance with minimum property standards. 7 C.F.R. § 1804.3(d) (1977). He prepares all loan documents. 7 C.F.R.

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[2] FmHA's organization is unique among federal agencies. FmHA has 2,200 county offices which are supervised by district offices and coordinated by a director for each state. Applications for loans from the FmHA are made at its 2,200 local county offices and processed by FmHA employees. *The United States Government Manual 1981/82*, pp. 105, 107. Applicants for home loan insurance programs administered by the Department of Housing and Urban Development (HUD) first apply to a HUD-approved private mortgage lender, which in turn applies to HUD. HUD employees never become personally involved in the loan process under HUD administered housing programs.

[3] Regulations cited are those in effect between August 16, 1976 and October 3, 1977, when Miss Neal applied for a Section 502 loan and her home was completed.

§ 1822.12-15 (1977). He even provides title clearance and legal services. 7 C.F.R. § 1822.9(d) and Part 1807 (1977). The county supervisor disburses loan proceeds.[4] 7 C.F.R. Part 1803 (1977); 7 C.F.R. § 1822.14 (1977). After the loan is completed and construction finished, he continues to service the borrower's account with FmHA. 7 C.F.R. Part 1861, Subpart A (1977). The county supervisor is also responsible for providing supervisory assistance to the borrower.

> Supervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect the interests of the Government in accordance with Subpart A of Part 1802 of this Chapter.

7 C.F.R. § 1822.7(a) (1977).[5]

> The basic objective of the Farmers Home Administration (FmHA) in making section 502 loans is to assist farmowners and other persons who will live in rural areas to obtain decent, safe, and sanitary dwellings and related facilities.

7 C.F.R. § 1822.2 (1977).

> The primary objectives of supervision are to assist . . . families to . . . obtain decent, safe, and sanitary housing . . . .

7 C.F.R. § 1802.2(b) (1977). This responsibility requires that the county supervisor closely inspect construction of housing built under the Section 502 rural housing loan program.

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[4] In order "to assure the correct expenditure of all or a part of loan" funds, the county supervisor is authorized to require the loan proceeds to be deposited in a supervised bank account. 7 C.F.R. § 1803.2 (1977). Withdrawals from supervised accounts are permitted only when countersigned by authorized FmHA personnel. 7 C.F.R. §§ 1803.5, 1803.7(b) (1977). Checks upon supervised accounts must be made to the appropriate payee, and must indicate the purpose of the expenditure. 7 C.F.R. § 1803.7(d)(1) (1977).

[5] FmHA cites part of this regulation out of context. (Pet. Br. 24) Regulations further provided that "supervisory assistance is especially important with families receiving initial FmHA loans who are relatively inexperienced. . . ." 7 C.F.R. § 1802.65 (1977).

> The County Supervisor will inspect development work as frequently as necessary to assure that construction and land development conforms with the plans and specifications.

7 C.F.R. § 1804.4(g)(3) (1977).

In October 1976, the Roane County FmHA office determined that Onilea Neal was eligible for a Section 502 rural housing loan. (C.A.App. 139) County supervisor S. Lane Parkison approved a loan of $21,170 for Miss Neal on June 9, 1977. (J.A. 54-55) After counseling with Miss Neal, he recommended that she buy a modular home "because the house that she was living in was falling down" and that she needed "immediate housing." (J.A. 115-116) He referred her to three modular home builders, including Home Marketing Associates, Inc. (hereinafter referred to as "Home Marketing"). (J.A. 115) She entered into contracts with Home Marketing for the construction of a modular house financed by FmHA. (J.A. 21-31) The contracts specified that the construction conform to FmHA approved plans and specifications; that changes in plans and specifications not be made by the contractor and borrower without FmHA's written approval; that FmHA inspect, examine and test all materials and workmanship; and that FmHA had the right to reject any defective materials and workmanship or to require its correction. (J.A. 27)

On August 8, 1977, before construction began, Onilea Neal executed a promissory note secured by deed of trust in favor of FmHA for repayment of the loan amount. (J.A. 32-46) Disbursements of the proceeds from the Section 502 loan were made in three installments during construction of Miss Neal's home: $2,170 on August 8, 1977; $11,500 on September 19, 1977; and $7,500 on September 30, 1977.[6] (J.A. 46)

Mary C. Wells, assistant county supervisor for FmHA, made inspections during construction of Miss Neal's home. Her

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[6] Disbursement of Miss Neal's Section 502 rural housing loan funds were made through a supervised bank account. See n. 4, *supra*.

reports indicated that inspections took place when the home was 2% completed (on August 24, 1977), 99% completed (on September 19, 1977), and 100% completed (on October 3, 1977). (J.A. 56-65) Nothing was noted on the reports except for the comment "Footings ok" on the first report. All inspection reports were signed by Mary Wells. Miss Neal did not sign the first two inspection reports, and there is no indication that she was given a copy of any of the inspection reports. The final inspection report was made three days *after* the final disbursement from the loan proceeds.[7]

The inspection reports are not appraisals. The inspection form (FmHA 424-12) requires the FmHA official to "itemize and describe the significant conditions observed to be at variance with the approved plans and specifications" and make "recommendations for correcting the deficiencies." (J.A. 56) If deficiencies had been previously reported, the FmHA employee is to check to see if they had been corrected. To assist the FmHA inspector, the inspection report form contains a checklist guide on the back. (J.A. 58-61) The county supervisor is not required to give inspection reports to the borrower or contractor.

As required by FmHA, Home Marketing executed a one-year builder's warranty which promised that the building was constructed in conformance with drawings and specifications approved by FmHA and minimum property standards published by the Department of Housing and Urban Development. The warranty applied to all workmanship, materials, and installation of equipment, including the heating system. The warranty specified the installation of a Chrysler heat pump, serial number 74152RS. (J.A. 47-51)

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[7] FmHA repeatedly asserts in its brief that Miss Neal purchased her home after the final inspection (and therefore relied on a misrepresentation). (Pet. Br. 10, 17, 21) These assertions, which are crucial to FmHA's argument, are false.

As required by regulation, Home Marketing submitted to FmHA plans and specifications for house plan Model 3B-1000B which purported to be for Miss Neal's dwelling. 7 C.F.R. Part 1804, Subpart A, Appendix C (1977). The plans for Model 3B-1000B did not include any layout of a heating and cooling system. (C.A.App. 148-152) However, specifications listed in "Descriptions of Materials" identified the heating system as electric, "General Electric, 220 Volts, output 15kw-Btuh," and identified the cooling equipment as "central system 2 ton air conditioner 15 kw." (C.A.App. 146)

On December 29, 1977, Onilea Neal notified FmHA and Home Marketing in writing that her heating system was not working. She had not received a warranty booklet or any instructions on the operation of the heat pump, and the name plate on the heat pump had been removed. (C.A.App. 14) In January 1978, Home Marketing informed Miss Neal that the heat pump unit installed in her home was a McGraw-Edison make. (C.A.App. 14) In February 1978, FmHA county supervisor Parkison discovered a tag inside the heat pump unit indicating a sizing of 10kw and 240 volts. In March 1978, after consulting with FmHA officials in Nashville, Tennessee, he declared that the unit was defective or undersized and requested Home Marketing to replace the unit. (C.A.App. 15)

On March 22, 1978, Earl Wayne Avery, FmHA State Director for Tennessee, and other FmHA officials inspected Onilea Neal's dwelling. In a letter to Home Marketing dated March 29, 1978, state director Avery confirmed that the heating and cooling system was defective, enumerated thirteen additional defects and requested their correction:

1. Porches were constructed of wood in lieu of masonry as shown on plans.

2. Rear service door was not exterior door with lights as shown on plan but appeared to be an interior hollow core without glass.

3. Vertical chase between bath and bedroom was not firestopped or sealed.

4. Bath was rearranged from plan.

5. No grade marks were observed on floor joist or roof truss lumber as required by MPS [Minimum Property Standards of HUD, adopted by regulation for use in FmHA construction.]

6. Roof truss does not appear to comply with approved design submitted with plan, staples used in lieu of nails. Truss design must conform to HUD criteria for trussed roof structure, 4950.2. The roof had a wavy appearance.

7. The unit was not properly caulked per MPS.

8. The exterior paint appeared to be of a low quality latex and was observed to be flaking off.

9. There was a broken floor joist under the front center bedroom.

10. The plumbing workmanship was observed to be poor.

11. The HVAC unit was observed to be a heat pump with 9.2 KW of auxiliary heater strips. Specifications called for General Electric 2-ton air conditioner and 15 KW of electric heat. Manufacturer of equipment could not be determined.

12. 1'' x 3'' bridging [between floor joints] was not observed, as shown in specifications.

13. Specifications call for 1/2'' sheetrock interior wall finish. Observed was approximately 1/8'' plywood paneling. This results in a wall assembly that does not meet MPS fire resistance ratings and span requirements for interior wall finish.

14. The manufacturer failed to certify that the unit was manufactured per approved plans and specifications, MPS and Structural Engineering Bulletin as required per approval letters.

(J.A. 52-53)

On December 28, 1979, over two years after Home Marketing and FmHA failed or refused to correct defects,[8] Onilea Neal

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[8] During 1978, repeated demands by Miss Neal and FmHA to correct defects were made upon Home Marketing with no results. In November 1978, Miss Neal filed a claim for compensation for con-

filed suit in the Circuit Court of Roane County, Tennessee, against the Department of Agriculture, the FmHA, and individual employees of FmHA together with the construction company and individual officers. She claimed damages caused by the negligent inspection and supervision of construction of her home by FmHA.[9] The government removed the case to the

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struction defects under 42 U.S.C. § 1479(c). FmHA did not respond to Miss Neal's compensation claim until May 1979. In June 1979, she requested a hearing upon her compensation claim. A hearing was held in July 1979. A hearing decision was made in September 1979 approving some of the defects as "justified." However, FmHA did not authorize payment for correction of "justified" defects. Instead FmHA made further demands upon Home Marketing to correct the defects. In May 1980, while Miss Neal's case was pending before the Sixth Circuit Court of Appeals, FmHA agreed to pay for correction of some of the defects. The first repairs to the heating system and plumbing were made in October 1980. When she filed this action, the elderly Miss Neal had lived in the house for two summers without air conditioning and was entering her third winter without an adequate source of heat.

Some, but not all, defects in Miss Neal's home have been corrected. The Court should be aware that in the course of correcting some defects, several other, perhaps more serious, defects have been discovered. When interior paneling was removed, workers discovered that Home Marketing has applied no exterior sheathing (as required by specifications) to the exterior walls between the studs and composite shingles. This defect exposed wiring and insulation in the exterior walls to outside weather conditions and caused excessive drafts. (Where the interior panels joined, daylight was visible from Miss Neal's living room.) It was also discovered that Miss Neal's house had not been anchored to the block foundation and is subject to high wind shift. Since these defects were discovered only this year, they may not be eligible for correction under Section 509(c), 42 U.S.C. § 1479(c).

[9] Miss Neal filed her administrative claim under the Federal Tort Claims Act on June 6, 1979. The office of General Counsel for the Department of Agriculture did not act upon the claim until January 9, 1980, after commencement of Miss Neal's action.

United States District Court for the Eastern District of Tennessee, Northern Division.

On February 5, 1980, the government filed a motion to dismiss the claims against the federal defendants for lack of subject matter jurisdiction and for failure to state a claim upon which relief could be granted. On February 26, 1980, the district court entered an order dismissing the claims against the federal defendants holding that the "plaintiff has failed to state facts upon which relief from the government defendants can be based."[10] (Pet. App. 26a) The court of appeals reversed, holding that Onilea Neal had stated facts sufficient to support a claim of negligent supervision and inspection of the construction of her home against the federal defendants. (Pet. App. 4a-18a)

SUMMARY OF ARGUMENT

The sole Question Presented by the government (Pet. Br. (I)) is whether a suit alleging negligent inspection by a Farmers Home Administration (FmHA) employee "is excepted from the coverage of the Federal Tort Claims Act as a "claim arising out of . . . 'misrepresentation' under 28 U.S.C. 2680(h)."[11] FmHA argues that the "misrepresentation" excep-

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[10] It should be noted that the district court made its ruling without benefit of the depositions of Wayne Humphrey (Home Marketing), S. Lane Parkison (FmHA county supervisor) and Mary C. Wells (FmHA assistant county supervisor) taken on February 7, 1980, and February 22, 1980. (C.A.App. 104, 116, 124) Mr. Humphrey's deposition was filed with the district court on February 27, 1980. The depositions of S. Lane Parkison and Mary C. Wells were filed on March 7, 1980. (C.A.App. 3) The district court remanded claims against Home Marketing to the Roane County Circuit Court where the case is awaiting trial. Home Marketing is no longer constructing homes and has been suspended from participating in FmHA rural housing programs.

[11] FmHA concedes that its supervision and inspection of construction of Miss Neal's home was done negligently. Moreover, FmHA does not contest the court of appeals' holding that FmHA voluntarily undertook a duty to competently supervise and inspect construction of Miss Neal's home.

tion to the waiver of governmental immunity should be interpreted broadly to exempt from tort liability any misfeasance or nonfeasance by FmHA's employees that involves communications (or lack of communication) in any form. Under the broad reading urged by FmHA, any tortious conduct by its employees which contain an element of communication would be exempt—even a claim based upon a motor vehicle operator's negligence in giving a wrong (misleading) turn signal.

FmHA's argument is contrary to the public policy and purpose of the Federal Tort Claims Act's broad waiver of immunity for tort actions. FmHA attempts to read immunity back into the Act through the "misrepresentation" exception without express enumeration by Congress. By characterizing the negligent inspections of its employees as "negligent misrepresentation," FmHA seeks to disavow its clear duty to Miss Neal and to avoid liability for negligent inspection of the construction of Miss Neal's home—liability clearly intended by Congress' waiver of governmental immunity.

FmHA's argument not only defies the sound public policy and purpose of the Federal Tort Claims Act, it ignores the clear allegations in Onilea Neal's complaint and facts in the record.[12] Miss Neal has *not* alleged and the facts *cannot* support a claim based upon the theory of "negligent misrepresentation." The allegations and facts *do* support a claim for breach of a duty to inspect construction of her home with due care which was voluntarily undertaken by FmHA or imposed upon FmHA by statute and regulations.

FmHA's argument depends entirely on its characterization of the final inspection report as identical to the appraisal statement which was the subject of *United States* v. *Neustadt*, 366

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[12] Even if some facts alleged in the complaint and in the record could be construed to be misrepresentation, whether there has been a misrepresentation, and what effect, if any, the misrepresentation had upon the parties' conduct, are fact questions which are more appropriately resolved after trial.

U.S. 696 (1961), and upon its assertion that Miss Neal purchased her home after receiving the final report. The record shows that the final payment from a supervised account to Home Marketing was made three days *before* the final inspection. Miss Neal did not sign or receive other reports. She was not required to receive any of them. She relied upon FmHA's actions—its competent supervision and inspection of construction of her home. The inspection reports themselves are *pro forma* and tangential to FmHA's duty to supervise and inspect construction with due care.

Although the court of appeals' decision holds that Miss Neal's complaint sufficiently alleges facts under which FmHA may be held liable for its negligence, there has been no trial on the merits. It is premature to rule on whether the evidence which may be presented at trial would support a finding of negligence by FmHA employees or on the measure of damages for which FmHA may be held liable.

ARGUMENT

I. FmHA OWED A DUTY TO SUPERVISE AND INSPECT CONSTRUCTION OF ONILEA NEAL'S HOME WITH DUE CARE.

FmHA does not dispute the court of appeals' holding that, by undertaking supervision and inspection of construction of Miss Neal's home, it was required to act carefully and with the exercise of due care.[13] It concedes that an FmHA employee negligently supervised and inspected construction of Onilea Neal's home. Although the government does not dispute an undertaking by FmHA to inspect construction of Miss Neal's

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[13] Having conceded a duty owing to Miss Neal, FmHA inconsistently argues that it is under no statutory duty to Miss Neal to competently inspect construction. It appears that the government makes the argument only because it was made in *United States* v. *Neustadt*, 366 U.S. 696 (1961). However, neither the facts nor the statutes involved in this case are similar to those in *Neustadt*.

home and admits negligence by an FmHA employee, it seeks to avoid liability solely through the misrepresentation exception to the Federal Tort Claims Act, 42 U.S.C. § 2680(h). (Pet. Br. (I))

Onilea Neal has alleged and the record shows that FmHA undertook to render technical services to her, engendered reliance on those technical services, breached its duty and caused damages. The FmHA's duty arose from its voluntary undertaking to render technical services. However, this duty can also arise under a statutory obligation imposed upon FmHA under Title V of the Housing Act of 1949 and particularly § 506 which was intended to benefit and protect rural, low-income persons like Onilea Neal.

A. FmHA Is Liable For Failure To Discharge A Duty Undertaken With Due Care.

One who undertakes, gratuitously or for consideration, to render services to another must perform his undertaking with due care. W. Prosser, *Handbook of Law of Torts*, Limited Duty, § 56 "Acts and Omissions" (4th ed. 1971); *Restatement (Second) of Torts*, § 323. A claim based upon the tort theory of voluntary undertaking is cognizable under the Federal Tort Claims Act. *Indian Towing Co.* v. *United States*, 350 U.S. 61, 69 (1955).

Onilea Neal's negligence claim is not predicated upon a "misrepresentation" by government employees—willful or negligent.[14] Her claim is based upon the negligent performance

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[14] 7 C.F.R. § 1804.4(g) (1977) does not require, or even suggest, that copies of the inspection reports (FmHA 424-12) be given to borrowers; nor does the present version of the construction inspection regulation, 7 C.F.R. § 1924.9 (1982). No statutory provision within Title V of the 1949 Housing Act requires that copies of reports of construction inspection and supervision by FmHA be given to borrowers. Unlike the appraisals in the *Neustadt* case, the inspection reports by FmHA in this case were incidental to supervision and inspection. In *Neustadt*, the "Statement of FHA Appraisal" was the

of undertakings to render services. *Restatement (Second) of Torts*, § 323. This theory of tort first requires that one undertake, either gratuitously or for consideration, to render services to another which he should recognize as necessary for the protection of the other's person or property. FmHA undertook to render technical services to Onilea Neal by supervising and inspecting of construction of her home. The FmHA county supervisor, his assistant and the contractor recognized that such supervision and inspection were necessary to assure that Miss Neal's home was constructed in conformance with FmHA approved plans and specifications.

County supervisor Parkison understood the statutory objective of the Section 502 home loan program and the purpose of supervision and inspection of construction:

> Q. [Croce] What's the objective of the section five-oh-two homeowner's loan program?
>
> A. [Parkinson] The objective is to provide decent, safe and sanitary housing to meet the needs of rural residents.

(J.A. 114).

Similarly, the county supervisor perceived his duties of supervision and inspection of construction as an integral process in achieving the objectives of the Section 502 home loan program:

> Q. And, let me ask you this, Mr. Parkison, Uh, don't you think some of these things, like inspections and warranties, contribute toward that objective?
>
> A. It's part of the, part of the loan process.

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end product. (Tr. 53, *United States* v. *Neustadt*, No. 533, 1960 Term) In this case, a safe, decent and sanitary home for Onilea Neal was the hoped for end product. Competent construction inspections were the primary means to achieve this goal. The reports were tangential to the actual construction inspections.

Q. Uh-huh. If the objective is to assure that people that, uh, in rural areas, to assure that they get safe, decent and sanitary housing, then part of the objective for making inspections and requiring warranties, and, you know, if there's something wrong, that you can withhold the money, and stuff like that, is to make sure that in fact those borrowers do get safe, decent and sanitary housing, is that correct?

A. That's correct.

(C.A.App. 120-121).

Thus, if the contractor desires a partial payment during construction, an FmHA employee inspects the construction and either approves or disapproves payment. Before the contractor may be paid, an FmHA official must authorize payment. (J.A. 26-27) The county supervisor admits that if defects had been discovered by proper inspection, corrections would have been required and/or payment to the contractor would not have been authorized.

The contractor also recognized that FmHA's inspections are to assure that the dwelling is constructed in accordance with plans and specifications, and that correction of defects does not depend upon any representation to the borrower.

Q. [Croce] So, if Farmers Home Administration isn't satisfied with either the amount of work done, or the quality or manner in which the work is done, then they'll either not pay or they'll withhold a certain portion of that check, is that correct?

A. [Contractor Humphrey] That would be my understanding, yes.

(J.A. 97).

Mary C. Wells, assistant county supervisor, made inspections during construction of Miss Neal's home. Miss Wells knew that these inspections were made to assure that the construction conformed to approved plans and specifications. (J.A. 91-92)

To achieve the purpose of supervision and inspection, FmHA need not (and was not required to) make a representation of any kind to Miss Neal or any other borrower. Indeed, if FmHA had discovered the defects in her home during construction and had responded only by telling her about them, such a response would be an abdication of its responsibility under the rural housing program. The entire scheme of construction inspection and supervision requires that *FmHA* act when it discovers defects during construction.[15] If FmHA's inspection had been done properly and with due care, *FmHA* could and should have prevented injury to Miss Neal by withholding funds from the contractor until the defects were corrected. Since no representation was made or required to be made, FmHA cannot assert that this action is now barred because of some *mis*representation.

Miss Neal alleged and was prepared to prove at trial that the construction inspections conducted by assistant county supervisor Mary Wells fell far short of a standard of due care of a reasonable person. Before or during inspections Mary Wells did not review or refer to the specifications, description of materials, or floor plans. (J.A. 79, 80) She did not refer to the checklist on the back of the inspection report form. (J.A. 82) She did not even attempt to inspect wiring, plumbing, firestopping, or the duct work for the heating or cooling system. (J.A. 82-88) She ignored the substitution of paneling for one-half inch sheet rock on interior walls without determining whether the substituted paneling complied with FmHA's requirement for flame spread rating. (J.A. 85-86) The evidence in the discovery deposition of Mary Wells is overwhelming that the construction inspections were incompetent.

The conduct of FmHA employees went beyond mere "nonfeasance." They controlled the entire home building proc-

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[15] The FmHA form contract states plainly that FmHA officials can and will "reject defective material and workmanship or require its correction." (J.A. 27)

ess by approving plans, preparing contract and loan documents, conducting inspections, and releasing payments during and after construction. Before construction, FmHA deposited the loan proceeds in a supervised account requiring signatures of an FmHA official and Miss Neal, and she was required to execute a promissory note and deed of trust in favor of FmHA. FmHA's actions did not stop once it had secured repayment of its loan and perfected its security interest. It undertook to supervise and insepct construction of Miss Neal's home. Mary Wells was the only person to conduct two of the inspections and no efforts were made to have Miss Neal participate. (J.A. 84) No effort was made to encourage Onilea Neal to independently inspect construction herself or to have anyone else inspect construction. Indeed, Miss Neal's financial eligibility for the Section 502 home loan demonstrates that she could not afford to have a private architect or engineer inspect for her. Her inexperience and lack of education—also anticipated under the Section 502 loan program—made it impossible for her to make, or be expected to make, a competent inspection on her own.

The conduct of FmHA engendered reliance upon it to assure that the home constructed for Onilea Neal conformed to plans and specifications. Therefore, FmHA was obligated to use due care to make certain that Miss Neal's home was properly constructed in conformance with plans and specifications—a duty which it breached.[16]

B. FmHA Is Liable For Failure To Discharge Its Duty Under Title V Of The 1949 Housing Act To Provide Reasonably Competent Technical Services To Onilea Neal.

In addition to a cause of action based on FmHA's undertaking to inspect construction of her home properly, Onilea Neal

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[16] Tennessee imposes liability for negligence in the discharge of a duty undertaken, even if gratuitously. *Nidiffer* v. *Clinchfield Railroad Company*, 600 S.W.2d 242, 246 (Tenn.App. 1980). *See also*, *Quinn* v. *Kansas City, M. & B. R. Co.*, 94 Tenn. 713, 30 S.W. 1036 (1895) (company who voluntarily undertook to provide medical care for employees had a duty to use due care in selection of physician).

can also establish a cause of action against FmHA for breach of duty arising under Title V of the 1949 Housing Act.

1. Tennessee imposes tort liability for failure to perform a duty which arises under legislation or regulations.

Tennessee imposes tort liability for failure to perform a statutory duty.[17] *Wise* v. *Morgan*, 101 Tenn. 273, 48 S.W. 971 (1898). A person seeking to hold another liable for negligently violating a statute or regulation must show that he is a person within the protection of the law and intended to be benefited. *Carter* v. *Redmond*, 142 Tenn. 258, 263, 218 S.W. 217, 218 (1920). Tennessee, in essence, has adopted *Restatement (Second) of Torts* § 286, which establishes when the duty of care arises under legislation or regulation.

2. Congress intended to benefit low-income persons such as Onilea Neal by providing government supervision and inspection of the construction of homes built under the Section 502 rural housing loan program.

Onilea Neal's complaint alleges substantial damages resulting from the failure of FmHA employees to exercise reasonable care in supervision and inspection of construction of her home. (C.A. App. 18). FmHA contends that the complaint should be dismissed because its duties under the Section 502 rural housing loan program, 42 U.S.C. § 1472, which include providing technical assistance to borrowers under Section 506(a), 42 U.S.C. § 1476(a), create no legal liability (duty) for failure to exercise reasonable care in their performance under any circumstances. Rather, FmHA claims that it supervises and inspects the construction of homes financed with its loans solely to protect the government's interest. The language of

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[17] "[T]he test established by the Tort Claims Act for determining the United States' liability is whether a private person would be responsible for similar negligence under the laws of the State where the acts occurred." *Rayonier, Inc.* v. *United States*, 352 U.S. 315, 319 (1957).

Section 506(a) and the legislative history of Title V of th 1949 Housing Act do not support this contention.

The distinction between the FHA and FmHA programs arose when Congress recognized that, unlike urban areas, rural areas (which have nearly two-thirds of the country's substandard housing) lack the financial institutions and technical expertise needed to finance and improve rural housing. 95 Cong. Rec. 4716-4717 (1949) (statement of Sen. McCarthy). Title V of the 1949 Housing Act, 42 U.S.C. § 1471 *et seq.*, established, among other things, several loan and technical services programs. It was enacted to ameliorate poor rural housing conditions. Recognizing the special needs of rural areas, Rep. Robert Jones (Ala.) explained the need for technical assistance during hearings on Title V of the 1949 National Housing Act:

> I would like to stress the importance of this technical service.
>
> Due to poor structures, poor plans, poor workmanship, or the lack of an over-all scheme for house improvement over the years, the remodeled or modernized house is not always convenient or comfortable. Improved plans and planning service, and education to the construction methods and elements of good planning, are very essential and are positively needed.

Housing Act of 1949: Hearings on H.R. 4009 Before the House Comm. on Banking and Currency, 81st Cong., 1st Sess. 178 (1949).

To meet the special housing needs of rural communities, Congress created much more than a loan program with traditional means to protect the government's security interest. 42 U.S.C. § 1472(b). Section 506 of the 1949 Housing Act states a congressional intent for the rural housing program that has no parallel in the 1934 National Housing Act:[18]

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[18] FmHA asserts that the "purpose of the requirement of supervision and inspection [of construction] in the 1949 Housing Act is the

> In addition to the financial assistance authorized in this subchapter, the Secretary is authorized to furnish, through such agencies as he may determine, to any person, including a person eligible for financial assistance under this subchapter, without charge or at such charges as the Secretary may determine, technical services such as building plans, specifications, construction supervision and inspection, and advice and information regarding farm dwellings and other buildings.

42 U.S.C. § 1476(a). This technical assistance was essential to fulfill Congress' purpose in enacting the 1949 Housing Act: "[T]he realization as soon as feasible of the goal of a decent home and a suitable living environment for every American family, . . . [including] governmental assistance . . . to provide adequate housing for . . . rural nonfarm families with incomes so low that they are not being decently housed in new or existing housing . . . ." 42 U.S.C. § 1441.

Sections 502 and 506 of Title V of the 1949 Housing Act impose on the Secretary three responsibilities when making rural home loans: First, he shall prescribe standards and make inspections to assure that decent, safe and sanitary housing is constructed; second, he shall protect the government's interest by securing all loans; and third, he is authorized to assist individual borrowers in attaining the objectives of the 1949 Housing Act by providing them with technical assistance as prescribed in Section 506(a), 42 U.S.C. § 1476(a).

The government contends that the language in Section 506(a) (42 U.S.C. § 1476(a)), and specifically the third sentence, was not meant to benefit borrowers such as Onilea Neal. Under the government's reasoning, however, the third sen-

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same as in the 1934 Act." (Pet. p. 10, n. 5) However, *no provision* within the 1934 National Housing Act authorizes the Secretary of Housing and Urban Development or FHA to furnish technical assistance including construction supervision and inspection to such borrowers if there were any. FmHA's assertion is not supported by statute.

tence under Section 506(a) would be superfluous. The first sentence of Section 506(a) provides that

> the Secretary shall require that all new buildings and repairs financed under this subchapter shall be substantially constructed and in accordance with such building plans and specifications as may be required by the Secretary.

The second sentence states:

> Buildings and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary.

Section 506(a) goes on to provide that in *addition* to financial assistance, the Secretary is to provide technical assistance to borrowers, including "construction supervision and inspection."

The first two sentences under Section 506(a) assure that new homes for low-income rural residents constructed with government funds are built properly. The third sentence prescribes technical assistance to be furnished to borrowers. The government's treatment of the third sentence of Section 506(a) ignores that sentence's plain language and relegates it to a function already performed by the first two sentences. To conclude that Congress intended only to protect the government's security interest is without statutory basis. This plain reading of Section 506(a) is confirmed by the legislative history.

Providing technical assistance to rural residents to obtain decent and safe housing was a concern of Congress from its initial consideration of rural housing legislation through its final adoption in 1949. In 1944 and 1945 the Subcommittee on Housing and Urban Redevelopment of the Senate Committee on Post-War Economic Policy and Planning conducted an extensive series of hearings examining housing in the United States. The subcommittee, in a unanimous report, recommended the "development of plans for a comprehensive attack on bad farm housing conditions." S. Rep. No. 84, 81st Cong., 1st Sess. (1949), *reprinted in* 1949 U.S. Code Cong. Serv. 1554.

Then Secretary of Agriculture, Claude R. Wickard was one of the main proponents testifying for increased government involvement in the rural farm housing area. He noted both the severe inadequacy of farm houses and the inability of farmers to cope with that problem:

> Research and education should be continued and expanded so that more farm families will become aware of the need for good housing, and so that they will have somewhere to turn for advice on design and materials. Cooperative buying of building materials should be encouraged; also use of timber, stone and gravel production on the farm. So should pooling of labor. More attention should be given to training architects in the specialized field of rural housing; and insofar as possible training builders and skilled workers. Such training also could be useful to farmers themselves; often they can supply much of the labor needed for improving their homes.

Post-War Economic Policy and Planning: Hearings Before the Subcomm. on Housing and Urban Redevelopment of the Senate Special Comm. on Post-War Economic Policy and Planning (Pt. 6), 78th Cong., 1st Sess. 1890 (1945).

Based on the subcommittee recommendations, Senators Taft (Ohio), Ellender (Louisiana), and Wagner (New York) introduced S. 1592 in late 1945. Among other provisions, the bill authorized the Secretary of Agriculture "[T]o furnish without charge, or such charges as the Secretary may determine, technical services such as building plans, specifications, construction supervision and inspection, and advice and information regarding rural housing." S. 1592, § 805. During hearings on S. 1592, then Secretary of Agriculture Clinton P. Anderson reaffirmed earlier testimony regarding the deplorable condition of farm housing, and addressed the role of technical assistance in relieving this problem: "The provision in S. 1592 for further research in house design, materials, and methods of construction, and for technical services and educational work, if enacted into law, should be helpful to the farmers . . . ." *General Housing Act of 1945: Hearings on S. 1592 before the Senate Comm. on Banking and Currency (Pt. 1)*, 79th Cong., 1st Sess. 801 (1945).

The Committee on Banking and Currency favorably reported S. 1592 with amendments, to the Senate on April 8, 1946. S. Rep. No. 1131, 79th Cong., 2nd Sess. (1946). The Senate report specifically interpreted § 805 of S. 1592 to be for the benefit of borrowers, not the protection of the agency:

> Section 805: In order to facilitate the provision of decent farm dwellings generally, this section authorizes the Secretary of Agriculture to furnish, without charge (or at appropriate charge), to all persons technical services such as building plans, specifications, construction supervision and inspection, and advice and information.

Id. at 44.

The bill, with amendments unrelated to technical and other special assistance to farmers, passed the Senate with little debate on the specific farm housing provisions. The House of Representatives, however, failed to complete consideration of housing legislation prior to the adjournment of the 79th Congress.

In the next session of Congress, Senate bill S. 866 was the successor to S. 1592. The technical assistance provisions of S. 1592 were now contained in § 1005 of S. 866.[19] The language of the provision itself, however, remained the same. 93 Cong. Rec. 2078 (1947) (analysis of Sen. Ellender).

The Committee on Banking and Currency favorably reported S. 866 without amendment to the Senate on April 24,

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[19] It is important to note that the Department of Agriculture was responsible for drafting the farm provisions of S. 866. As Senator Taft stated during the 1947 hearings on S. 866: "This particular plan was proposed by Secretary Anderson. We put it up to the Department of Agriculture to come in with a proposal." *Housing: Hearings on S. 287, S. 866, S. 701, S. 801, S. 802, S. 803, and S. 804 before the Senate Comm. on Banking and Currency*, 80th Congress, 1st Sess. 17 (1947). Later testimony by Agriculture officials continued to emphasize their desire to benefit and protect borrowers by providing technical assistance, incuding construction supervision and inspection. See testimony of Assistant Secretary Brannan, *et al.*, *infra*.

1947. S. Rep. No. 140, 80th Cong., 1st Sess. (1947). In that report the committee again quoted the language of the 1946 analysis of § 805 of S. 1592. *Id.* at 47. The intent of Congress in providing technical assistance under the farm housing legislation remained the same.

Later, before the House, Assistant Secretary of Agriculture, Charles F. Brannan, testified concerning the technical assistance section of S. 866.

> [It] would permit the Department to go further than it has in the past. Suppose a farmer wants to remodel his house or build a new one. He would probably have tentative plans in mind. But under the Act, there would be competent architects and engineers available to assist the farmer in planning his house and to give him some guidance as he proceeded.

General Housing: Hearings on S. 866 before the House Comm. on Banking and Currency, 80th Cong., 2nd Sess. 293 (1948).

Under H.R. 6888, favorably reported by the House Committee on Banking and Currency, language pertaining to technical assistance to farmers mirrored that of S. 866. H. Rep. No. 2340, 80th Cong., 2nd Sess. 28 (1948). Consideration of H.R. 6888, however, expired at the end of the 80th Congress without having reached a vote in the full House.

In 1949, both the Senate and House quickly introduced housing bills reflecting the housing legislation considered by the previous Congresses. Congressional bills S. 1070 and H.R. 4009 both retained the farm housing technical assistance sections. The Senate report explained the farm housing provisions of S. 1070:

> A special type of financial assistance designed specifically to meet the problems of the farmers who cannot get credit elsewhere and of research and technical services, pointed toward more efficient and more economical construction of farm buildings, must be undertaken by the Government. The authority for such assistance is provided in Title IV of this bill.
>
> . . . .

> The bill also contains an extremely necessary and desirable authorization which permits the expansion of technical services, such as plans, specifications, construction supervision and inspection, and advice and information in the Department of Agriculture, and authorizes the Secretary to conduct a program of research with a view to reducing costs, and to make market studies and assemble data in the farm-housing field.

S. Rep. No. 84, 81st Cong., 1st Sess. 25 (1949).

The Senate Committee on Banking and Currency issued a supplemental report. S. Rep. 84 (Pt. 2), 81st Cong., 1st Sess. (1949). In reference to the technical services and research section of S. 1070, the supplemental report stated:

> This section [406/technical services and research] provides that all new buildings constructed, or repairs made with financial assistance under this title shall be substantially constructed in accordance with such plans and specifications as may be required by the Secretary. This section also authorizes the supervision and inspection of construction to the extent which may be found necessary for accomplishing the purposes of this title and for the preservation of the Government's security interest. The extent of the requirements for building plans, supervision, and inspection would depend upon the character of the construction and the amount of the loan. These provisions are somewhat more specific than the related provisions in the predecessor bill (S. 138) [S. 138 mirrored the language of earlier bills discussed] as originally introduced.

Id. at 20.[20]

The supplemental report further analyzed § 406:

> The Secretary would also be authorized under this section to furnish, without charge or at such charges as he may determine, to any person, including any person eligible for financial assistance under this title, building plans, specifications, construction supervision, advice and in-

[20] FmHA cites the third sentence of this quotation out of context. (Pet. Br. 23)

> formation, and similar technical services regarding farm dwellings and other buildings. In order to assure that such services are rendered consistent with the primary purpose of this bill, specific authorization for research and technical studies is contained in this section.

Id. at 20.

For the first time, in this Senate supplementary report, the two different purposes of providing technical assistance to farmers was addressed—the construction of the home itself ("the purposes of this title") and the "government's security interest." *Id.*

The "somewhat more specific" provisions in S. 1070 referred to in the supplemental report consisted of additional language attached to the beginning of former bill provisions:

> In connection with financial assistance authorized in §§ 401-404, inclusive, the Secretary shall require that all new buildings and repairs financed under this title shall be substantially constructed and in accordance with such building plans and specifications as may be required by the Secretary. Buildings and repairs constructed with funds advanced pursuant to this title shall be supervised and inspected, as may be required by the Secretary, by competent employees of this Secretary.

S. 1070, § 406. This language is substantially the same as the current language in the first two sentences of Section 506(a), 42 U.S.C. § 1476(a).

It is significant that this new language in S. 1070, § 406 was *added* to the language of the previous bills which had been under consideration for a number of Congressional sessions. The former language remained intact as part of the eventually enacted legislation—the third sentence of Section 506(a). 42 U.S.C. § 1476(a). The additional language also became part of the enacted legislation. Therefore, remarks on the former bills' language (third sentence of 42 U.S.C. § 1476(a)) remain pertinent. These show that the primary purpose for technical assistance was to benefit and protect borrowers, and refute FmHA's

bald assertion to the contrary.[21] The new language in the technical assistance provisions as reported by the supplemental Senate report did not override the purpose in providing technical assistance to farmers and other rural residents for obtaining safe and decent housing.

The House report on the proposed farm housing legislation also emphasized the construction aspects of the technical assistance to be provided to the farmers:

> The bill also provides for technical assistance by the Department of Agriculture in farm-home design and construction, and authorizes the Secretary of Agriculture to conduct research directed toward lowering the cost of farm housing and to assemble data and market information in this field.

H. Rep. No. 590, 81st Cong., 1st Sess. 31 (1949). The 1949 hearings on housing legislation contained several strong statements which underscored that technical assistance, including construction supervision and inspection, was authorized to benefit borrowers in obtaining safe, decent and sanitary housing. *See, e.g.*, Statements of Secretary of Agriculture Charles F. Brannan and Wayman C. Smith, Assistant Chief, Bureau of Agricultural Economics, Department of Agriculture, *General Housing Legislation: Hearings on S. 138, S. 685, S. 686, S. 709, S. 712, S. 714 and S. 757 before a Subcomm. of the Senate Comm. on Banking and Currency*, 81st Cong., 1st Sess. 205, 209 (1949). See also, Statement of Senator J. Allan Frear (Delaware), 95 Cong. Rec. 4717 (1949).

The farm provisions of the Housing Act were enacted on July 15, 1949, as part of the 1949 Housing Act. See Congressional Code, 1949 Act, Public Law 171, Chapter 338, pp. 429-430,

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[21] In recent regulatory changes, FmHA states that inspections are solely to protect its security interest. 45 Fed. Reg. 39787, 39792 (1980). FmHA asserts that the changes "were intended to clarify preexisting law on this issue." (Pet. Br. 5, n. 1) No authority is cited for this assertion because there is none.

codified at 42 U.S.C. § 1471 *et seq.* Within two weeks after enactment, on July 27, 1949, a handbook on information on provisions of the Housing Act was published by the Senate. *The Housing Act of 1949 What It Is and How It Works: A Handbook on Information on Provisions of the Act and Operations under the Various Programs* (1949) (printed for the use of the Senate Comm. on Banking and Currency). The Handbook explained:

> A separate section (506) has been set up under title V to provide for farm research and technical services. This is to further permit the Secretary of Agriculture to have overall supervision of the entire rural phases of this housing bill. Section 506 authorizes the Secretary to furnish, without charge, or at such charges as he may determine, technical services such as building plans, specifications, construction supervision and inspection, and any necessary advice or information on rural dwellings or other farm buildings.

Id. at 24. In 1961, Congress extended the provisions of Title V of the 1949 Housing Act to include low-income rural residents. Pub. L. 87-70, § 803(a), *codified at* 42 U.S.C. § 1471.

In summary, the legislative history of the 1949 Housing Act demonstrates that, unlike the 1934 National Housing Act involved in *Neustadt*, Congress intended that technical services be provided to benefit and protect rural borrowers and to provide adequate security for the government's direct loan. Both purposes are prominently and explicitly discussed throughout the legislative history and cannot be separated. The government's attempt to seize on the security purpose of technical assistance ignores the Congressional intent expressed throughout its deliberations on the 1949 Housing Act.[22]

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[22] On March 24, 1976, the nonpartisan Congressional Research Service (CRS) published "*The Farmers Home Administration: Its Operation and Programs*," by George Gilbert and Nancy Smith. The Report stated that the Housing Act of 1949

> [r]equired certain quality of construction. Authorized supervision and inspection of buildings and repairs. Authorized free

Onilea Neal resides in a rural Tennessee County within the Southern Appalachian Mountains. Since she could not find safe, decent and sanitary housing which she could afford to rent or buy through conventional financing, she sought assistance from FmHA. She had a limited education and no prior experience in building or buying a home. Onilea Neal needed more than financial assistance. As a "lender of last resort," Congress intended FmHA to give Miss Neal more than financial assistance. FmHA had a duty to provide Onilea Neal with the technical assistance needed to obtain safe, decent and sanitary housing. Onilea Neal epitomizes the kind of person Congress intended to benefit under Title V of the 1949 Housing Act and the rural housing loan program administered by FmHA.

II. ONILEA NEAL'S NEGLIGENCE CLAIM IS NOT BARRED BY THE MISREPRESENTATION EXCEPTION TO THE FEDERAL TORT CLAIMS ACT, 28 U.S.C. § 2680(h).

The purpose of the Federal Tort Claims Act is to waive the government's traditional all-encompassing immunity from tort action. *Rayonier, Inc.* v. *United States*, 352 U.S. 315, 319 (1957). In light of its broad purpose and policy, this Court has steadfastly refused to read exemptions into the Act beyond those expressly enumerated by Congress.

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technical services such as building plan specifications, supervision and inspection and advice and information regarding farm dwellings and other buildings.

Id. at 68. It also stated:

> Rural communities and businesses often need technical and managerial assistance both in planning their undertakings and in operating the facilities and businesses after they are begun. In such cases, protecting FmHA's interest as well as the interest of borrowers is largely dependent on FmHA's ability to provide its clients with personal counseling and supervision both prior to and after the loan is made. . . .

Id. at 13.

> In argument before a number of District Courts and Courts of Appeals, the Government relied upon the doctrine that statutes waiving sovereign immunity must be strictly construed. We think that the congressional attitude in passing the Tort Claims Act is more accurately reflected by Judge Cardozo's statement in *Anderson* v. *Hayes Construction Co.*, 243 N.Y. 140, 147, 153 N.E. 28, 29-30: "The exemption of the sovereign from suit involves hardship enough where consent has been withheld. We are not to add to its rigor by refinement of construction where consent has been announced.

United States v. *Aetna Casualty & Surety Co.*, 338 U.S. 366, 383 (1949).

Attempts to expand governmental immunity through vague and irrational distinctions conflict with Congressional intent to waive immunity from tort actions.

> There is nothing in the Tort Claims Act which shows that Congress intended to draw distinctions [like governmental and non-governmental activity] so finespun and capricious as to be almost incapable of being held in the mind for adequate formulation.

Indian Towing Co. v. *United States*, 350 U.S. 61, 68 (1955).

> The broad and just purpose which the statute was designed to effect was to compensate the victims of negligence in the conduct of governmental activities in circumstances like unto those in which a private person would be liable and not to leave just treatment to the caprice and legislative burden of individual private laws. Of course, when dealing with a statute subjecting the Government to liability for potentially great sums of money, this Court must not promote profligacy by careless construction. Neither should it as a self-constituted guardian of the Treasury import immunity back into a statute designed to limit it.

350 U.S. at 68-69.

Onilea Neal's complaint alleges substantial damages as a result of the failure of FmHA employees to exercise reasonable care in supervision and inspection of construction of her home. (J.A. 12). FmHA contends that although Miss Neal's claim is

stated as negligence, her claim is in fact based on the tort theory of "negligent misrepresentation." In essence, FmHA argues that this Court should give the "misrepresentation" exception within the Tort Claims Act (28 U.S.C. § 2680(h)) an all-encompassing, broad interpretation which would exempt from tort liability any operational malfunction by the government that involves communications in any form. Such an attempt should be denounced on policy reasons alone.[23] Moreover, in the instant case, the FmHA's characterization of Miss Neal's claim as "negligent misrepresentation"[24] cannot be supported by the facts alleged in the complaint and record.

A. The Allegations In The Complaint And Facts In The Record Do Not Support A Claim Under The Theory Of Negligent Misrepresentation.

Onilea Neal stated that she "relied upon employees of Farmers Home Administration to assist me to purchase a home and to make sure the house was built right." (C.A. App. 85). Miss

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[23] In this case, the government asserted the misrepresentation exception by motion to dismiss under Fed.R.Civ.P. 12(b)(6) prior to discovery and trial. Because whether a claim lies in misrepresentation or negligence is a fact question, it is more appropriate to resolve this question at trial or, at a minimum, after all discovery is completed. This is in keeping with the judicial policy disfavoring motions to dismiss for failure to state a claim "unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley* v. *Gibson*, 355 U.S. 41, 45-46 (1957).

[24] Tennessee has adopted the tort theory of negligent misrepresentation. *Tartera* v. *Palumbo*, 224 Tenn. 262, 453 S.W.2d 780 (1970). The essential elements of negligent misrepresentation are: (1) the supplying of false information in the course of business, profession or employment in which the supplier of information has a pecuniary interest; (2) justifiable reliance upon the information by the person receiving the information; and (3) pecuniary loss suffered by the person receiving the information through reliance. *Restatement (Second) of Torts*, § 552 "Negligent Misrepresentation."

Neal claimed that FmHA negligently inspected and supervised the construction of her home. (J.A. 12) She did not claim that FmHA supplied information which was false, that she relied upon any false information, or that she suffered any loss through reliance upon the false information.

FmHA contends that the "gravamen"[25] of Miss Neal's negligence claim is negligent misrepresentation. The facts alleged and evidence in the record cannot support such a claim.

FmHA cites the final inspection report dated October 3, 1977, as the false information supplied to Onilea Neal. Although the final inspection report was signed by Onilea Neal, the record contains no indication that the report was given to Miss Neal. No evidence suggests that the inspection report was signed by Miss Neal *before* or *after* Mary Wells or what was stated, if anything, when the final inspection report was executed.

Even if the October 3rd inspection report was communicated to Miss Neal, nothing in the record or pleadings shows that she relied upon the report in the course of her dealings.[26] Onilea Neal executed the promissory note and deed of trust in favor of FmHA on August 8, 1977. (J.A. 32-46) All disbursements from the proceeds of the Section 502 loan were made before October 3, 1977: $2,170 on August 8, 1977; $11,500 on September 19, 1977; and $7,500 on September 30, 1977 (total of $21,170). (J.A. 46) Miss Neal could not have relied upon the final inspection report in executing the promissory note and deed of trust and in allowing disbursements of the loan proceeds.

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[25] FmHA's "gravamen" argument is reminiscent of the "gist of the claim" argument rejected by the Court in *United States* v. *Neustadt*, 366 U.S. 696, 703 (1961).

[26] The government repeatedly states that Miss Neal purchased the house *after* an FmHA inspector certified that the construction was proper. (Pet. Br. 10, 17, 21, n. 11) This is a misstatement of fact. If the record was unclear about when the purchase was completed (which it is not), such a fact could best be established by a trial on the merits.

This fact situation fails to meet an essential test necessary to a finding of liability upon a false representation.

> The false representation must have played a material and substantial part in leading the plaintiff to adopt his particular course; and when he was unaware of it at the time he acted, or it is clear that he was not in any way influenced by it, and would have done the same thing without it for other reasons, his loss is not attributed to the defendant.

W. Prosser, *Handbook of Law of Torts*, Misrepresentation, § 108 "Reliance" (4th ed. 1971). No allegation made and no facts presented demonstrate that Onilea Neal's actions were predicated upon the inspection reports themselves. FmHA's attempt to characterize Miss Neal's claim as negligent misrepresentation is an illogical attempt to merge misrepresentation with other kinds of tortious misfeasance or nonfeasance. *See, e.g., Ware* v. *United States*, 626 F.2d 1278, 1281-83 (5th Cir. 1980); *Ingham* v. *Eastern Airlines, Inc.*, 373 F.2d 227, 239 (2nd Cir. 1967), *cert. denied*, 389 U.S. 931 (1967). *See generally*, W. Prosser, *Handbook of Law of Torts*, Misrepresentation, § 105 "Remedies for Misrepresentation" (4th ed. 1971).

B. FmHA Negligently Breached Its Duty To Inspect Construction With Due Care.

As in *Indian Towing*, the instant case involves negligence at the "operational level" of governmental activity. In *Indian Towing*, the government argued "that there can be no recovery based on the negligent performance of the [unique governmental] activity itself, the so-called 'end-objective' of the particular governmental activity." 350 U.S. at 66. The Court rejected this reasoning since "all Government activity is inescapably 'uniquely governmental' in that it is performed by the Government." 350 U.S. at 67. The Court cast aside the "finespun and capricious" distinction urged by the government. 350 U.S. at 68. The Court concluded:

> The Coast Guard need not undertake the lighthouse service. But once it exercised its discretion to operate a light on Chandeleur Island and engendered reliance on the

> guidance afforded by the light, it was obligated to use due care to make certain that the light was kept in good working order; and, if the light did become extinguished, then the Coast Guard was further obligated to use due care to discover this fact and to repair the light or give warning that it was not functioning. If the Coast Guard failed in its duty and damage was thereby caused to petitioners, the United States is liable under the Tort Claims Act.

350 U.S. at 69.

Following *Indian Towing*, the Court reviewed the scope of the misrepresentation exception to the waiver of governmental immunity from tort claims. In *United States* v. *Neustadt*, 366 U.S. 696 (1961), the Court was confronted with a narrow issue:

> [W]hether the United States may be held liable, . . ., to a purchaser of residential property who has been furnished a statement reporting the results of an inaccurate FHA inspection and appraisal, and who, *in reliance thereon, has been induced by the seller to pay a purchase price in excess of the property's fair market value.*

366 U.S. at 697-698 (emphasis added).

In *Neustadt*, the plaintiff, an attorney, sought to purchase a 16 year old home. Mr. Neustadt made an offer to purchase a home contingent upon obtaining financing through a private mortgage loan insured by the Federal Housing Administration (FHA) pursuant to Section 203 of the Housing Act of 1934 (12 U.S.C. § 1709).[27] (Tr. at 15-16, *United States* v. *Neustadt*, No. 533, 1960 Term) In connection with its issuance of a conditional

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[27] Section 203 of the National Housing Act of 1934, as amended, 12 U.S.C. § 1709(a), provided that the "[Federal Housing Commissioner] is authorized, upon application by the *mortgagee*, to *insure* as hereinafter provided any mortgage offered to him [Commissioner] which is eligible for insurance as hereinafter provided, and, upon such terms as the [Commissioner] may prescribe, to make commitments for the *insuring* of such mortgages prior to the date of their execution or disbursement thereon. . . ." [Emphasis added.]

insurance commitment to the private lender,[28] FHA made an inspection of the property to determine whether it was eligible for FHA mortgage insurance and to assign an appraised value establishing the maximum amount of mortgage insurance obtainable. 366 U.S. at 697. Finding no obvious defects and fixing a value on the property, FHA issued an insurance commitment to the mortgagee, and pursuant to 12 U.S.C. § 1715q, the seller of the home provided Mr. Neustadt with a copy of the appraisal. (Tr. at 16, 53, *United States* v. *Neustadt*, No. 533, 1960 Term) The original offer of Mr. Neustadt was higher than the FHA appraisal and Mr. Neustadt withdrew his offer. Mr. Neustadt made a second, lower offer which was refused by the seller. Mr. Neustadt's third offer (conditioned upon the FHA appraised value) was accepted by the seller. (Tr. at 16-18, 54, *United States* v. *Neustadt*, No. 533, 1960 Term) Several days after Mr. Neustadt took possession of the property, the foundation began to settle in an unusual manner, causing substantial damage to the interior and exterior walls.[29] 366 U.S. at 698-99. Mr. Neustadt claimed that he had *relied* on the FHA *appraisal* in purchasing the house and commenced an action against FHA, seeking to recover the difference between the market value of the damaged house and the FHA appraised value. 366 U.S. at 701.

The government conceded that the inaccurate FHA appraisal resulted from a negligent inspection and that Mr. Neustadt relied upon that appraisal in purchasing a home for more than its actual market value. 366 U.S. at 702. The Court concluded that Congress intended the misrepresentation exception

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[28] An application for FHA mortgage insurance may be made only by a *financial institution* approved as a mortgagee by the FHA. Section 203(a), National Housing Act of 1934, 12 U.S.C. § 1709(a).

[29] The cause of the damage could not be ascertained by inspection of building repair contractors. Only after the original builder and four FHA field inspectors made a core drilling through the basement concrete floor was it discovered that the subsoil conditions were causing damage to walls and ceilings. 366 U.S. at 700.

under 28 U.S.C. § 2680(h) to include negligent as well as willful misrepresentation. 366 U.S. at 702. The *facts* as alleged by Mr. Neustadt and agreed to by the government made out a classic negligent misrepresentation claim: 1) The supplying of false information; 2) reliance upon the false information by the person receiving it; and 3) loss suffered by the person receiving the information through reliance. Mr. Neustadt's claim was barred under the misrepresentation exception to the Tort Claims Act.

The Court also rejected the assertion that Section 226 of the National Housing Act of 1934 (12 U.S.C. § 1715q)[30] gave rise to a specific governmental duty to protect prospective home purchasers by requiring a careful appraisal by FHA. 366 U.S. at 705. The Court carefully examined the legislative history of the National Housing Act of 1934, especially Section 226, (12 U.S.C. § 1715q), which required that a copy of the appraisal be given to the home purchaser. The Court concluded that "the primary and predominant objective of the appraisal system was the 'protection of the Government and its insurance funds.' " 366 U.S. at 709. Moreover, even if the government had breached a "specific [statutory] duty" to Mr. Neustadt, his claim based on reliance upon an inaccurate FHA appraisal was barred under the "misrepresentation" exception. 366 U.S. at 706-707. That is, the *facts* in *Neustadt*, regardless of how the governmental duty arose, placed the claim under the misrepresentation exception.

The Court in *Neustadt* was careful to note that its holding did not conflict or impair the authority of *Indian Towing*. 366 U.S. at 711, n. 26. The distinctions between *Neustadt* and *Indian Towing* were both factual and statutory.

First, the government in *Indian Towing* was the only operator of lighthouses. In *Neustadt*, the FHA did not make loans

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[30] Section 226 of the National Housing Act of 1934, 12 U.S.C. § 1715q, requires a builder or seller to deliver a copy of the FHA appraisal to the prospective purchaser prior to sale.

and did not supervise or inspect the construction or purchase of homes. The plaintiff in *Indian Towing* had no other guidance for its vessels. The government was the sole source of guidance and engendered reliance by operators of sea vessels. In *Neustadt*, the plaintiff was able to purchase a home in the private market place, engaged in arms length bargaining with a private seller and had various means of financing that purchase—through FHA, V.A. or conventional mortgage arrangements. The government was not the source of financing and certainly not the only source for mortgage insurance or house appraisals. The government related to the purchaser only through the mortgagee and did not engender reliance by the purchaser upon its appraisal. (Tr. 53, *United States* v. *Neustadt*, No. 533, 1960 Term)

Onilea Neal's claim falls squarely within the *Indian Towing* factual distinctions.[31] She had to demonstrate that she could not get financing from any other source before she could qualify for a FmHA Section 502 home loan. All alternative home financing had to be eliminated before she was eligible for a FmHA Section 502 home loan.

The FmHA county supervisor knew that Onilea Neal was living in inadequate housing which was literally falling down on her. He directed Onilea Neal to builders of modular homes who

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[31] The distinctions between Miss Neal's case and Mr. Neustadt's case are specific and numerous. FmHA determined Miss Neal's eligibility for a direct loan; FHA made no determination concerning Mr. Neustadt's qualifications to obtain financing. Miss Neal has low income and little education; Mr. Neustadt was a lawyer who purchased a $24,000 house and obtained a private loan of $18,000 after a down payment of $5200. FmHA approved a loan to Miss Neal for the purpose of building her home; FHA appraised a 16-year old house with no idea of when it might be sold or to whom. FmHA undertook to inspect the construction of Miss Neal's home and had authority to reject work and have it corrected; FHA merely set an appraised value which was for insurance purposes only and not intended to establish a sales price. Finally, it is important to recognize that Mr. Neustadt had a trial; Miss Neal has not yet had her day in court.

had been approved by FmHA. After Miss Neal had selected a modular home model, the plans and specifications had to be approved by FmHA.

On August 8, 1977, Onilea Neal executed a promissory note payable to FmHA in the amount of the Section 502 loan. The amount of loan and therefore the price of the house which Miss Neal could afford were dictated by funds available from FmHA and her ability to repay. She executed a deed of trust to FmHA to secure the promissory note.

FmHA started to disburse proceeds of the loan. The first disbursement was in the amount of $2,170 on August 8, 1977—the same day that the note and deed of trust were executed. At this point Onilea Neal was committed and no longer had any choice concerning the purchase of a home or her obligation to repay the loan. There never was any arms length bargaining.

FmHA undertook a first inspection of the construction on August 24, 1977, when the foundation footings were complete. It noted nothing irregular. There is no evidence that Miss Neal was given a copy of the inspection, participated in the inspection, or told to have inspections done herself. Since Miss Neal had to have very little income to qualify for a loan, she was inherently unable (and it is inconceivable that FmHA would expect her to be able) to afford a private consultant.

A second inspection occurred on September 19, 1977. Again no irregularities were noted. Still, FmHA made no efforts to encourage or to require Onilea Neal to inspect the construction or to hire anyone else to inspect. There is no evidence that Miss Neal was aware of the second inspection. Another disbursement in the amount of $11,500 was made on the same day as the second inspection.

The final disbursement of $7,500 was made on September 30, 1977. The final inspection by the assistant county supervisor was made three days later on October 3, 1977. She noted no irregularities on the inspection form or to Onilea Neal. Although Miss Neal signed the final inspection, she could not

have relied upon it to approve the final disbursement three days earlier.

FmHA's inspections were not to establish an appraised value. They were made to obtain a safe, decent and sanitary home for Onilea Neal. FmHA had agreed to make a loan to Miss Neal since she could not obtain any other source of financing and could not obtain other decent, safe housing within her financial means. FmHA knew that Miss Neal had never been a homeowner before, was not experienced in home building, had a limited education and income, and desperately needed decent, safe and sanitary shelter. FmHA recommended a home builder. Miss Neal signed a promissory note and deed of trust before construction began. FmHA knew that the home to be constructed was for Miss Neal, no one else. Given these facts, it is clear that FmHA did not undertake inspections merely for its own benefit.

FmHA's actions in this case are analogous to the activities of the Coast Guard in *Indian Towing*. Once FmHA employees undertook to inspect and supervise the construction of Miss Neal's home, and engendered total reliance upon their technical assistance, they were obligated to use due care to make sure that the construction of her home was proper and in conformance with plans and specifications. If the home was not being constructed properly, FmHA was obligated to discover this fact and to correct it. The reports themselves were tangential to competent inspections. FmHA failed in its duty undertaken and damage was caused to Onilea Neal. It is therefore liable under the Tort Claims Act.

Courts have soundly rejected similar attempts by the government to avoid liability for its negligent performance of operational tasks. For example, in *Ingham* v. *Eastern Air Lines, Inc.*, 373 F.2d 227 (2nd Cir. 1967), *cert. denied*, 389 U.S. 931 (1967), the government argued that "the negligent failure of its employees to convey weather information was a 'misrepresentation' which cannot serve as a basis for liability." 373 F.2d at 238. The circuit court, relying upon *Indian Towing*, rejected the government's attempt to bring its employees'

negligence within the misrepresentation exemption. As the circuit court noted:

> The government concedes there are diverse kinds of negligence which could be said to involve an element of misrepresentation but which Congress did not intend to be encompassed by the exception contained in § 2680(h) [misrepresentation].

373 F.2d at 239. The circuit court concluded

> the government's reading of the misrepresentation exception is much too broad, for it would exempt from tort liability any operational malfunction by the government that involved communications in any form.

Id.

In *Ingham*, the government employees had a two-fold duty: To conduct a reasonably competent effort to discover weather conditions and to convey those weather conditions. A similar two-fold duty was imposed upon the Coast Guard in *Indian Towing*. That some communication is involved is immaterial.

> [W]here the government, on the basis of facts which it is chargeable with ascertaining by a proper examination, has a duty to perform in addition to the duty of disclosing those facts, negligence in the conduct of such examination which results in a failure to perform the additional duty is not covered by the § 2680(h) exception.

Hungerford v. *United States*, 307 F.2d 99, 103 (9th Cir. 1962). *See also*, *Beech* v. *United States*, 345 F.2d 872, 874 (5th Cir. 1965).

The Court's rationale in *Indian Towing* guided the court of appeals in this case below. The court of appeals properly rejected FmHA's characterization of Onilea Neal's claim.

> Plaintiff's [Miss Neal's] claim . . . is based not on misrepresentation, as in the issuance of a false or inaccurate appraisal report, but rather on FmHA's failure to use due care in a voluntary undertaking, i.e., inspection and supervision of the construction of her house.

(Pet. App. 17a). The court of appeals' finding is fully supported by the allegations in the complaint and facts in the record. Its

holding also comports with two important policies which govern claims under the Federal Tort Claims Act: The policy of not imputing immunity when Congress has not clearly enumerated an exemption from liability; and the policy that vague and irrational distinctions not be drawn to frustrate the purpose of the Act.

III. ONILEA NEAL STATES A CLAIM FOR RELIEF

The district court dismissed Onilea Neal's complaint for failure to state a claim for relief. Fed.R.Civ.P. 12(b)(6). The court of appeals reversed. Miss Neal has had no opportunity to fully present evidence in support of her claim.

The factual allegations of Miss Neal's complaint must be taken as true. *Radovich* v. *National Football League*, 352 U.S. 445, 448 (1957). The "complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of [her] claim which would entitle [her] to relief." *Conley* v. *Gibson*, 355 U.S. 41, 45-46 (1957).

The alleged facts and evidence in the record show that FmHA undertook to supervise and inspect the construction of Miss Neal's home and did so negligently. FmHA concedes this conclusion. However, it makes misstatements of facts to support a theory that Miss Neal's claim is barred under the misrepresentation exception in the Federal Tort Claims Act.

The government states that Miss Neal purchased her home "*after* an FmHA inspector had certified that the construction was satisfactory." (Pet. Br. 10) (Emphasis added.) The government also asserts:

> Based on FmHA's certification that the construction was satisfactory, the loan money was released to respondent [Miss Neal] and she proceeded to purchase the house from the contractor.

(Pet. Br. 17) The government further states that the injury to Miss Neal "would still have occurred unless that information [defects in construction] was conveyed to her" since *she* paid

the money to the contractor. (Pet. Br. 21, n. 11) These assertions are not supported by any facts in the record and misstates facts that are in the record.

Onilea Neal entered into a contract for the purchase of her home, executed a promissory note to repay FmHA, and gave FmHA a deed of trust on her future home to secure its note *before* any construction began. *Supra*, p. 5. The first disbursement of loan proceeds was made *before* the first inspection. The final disbursement was made *before* the final inspection. *Supra*, p. 5-6. No facts in the record or alleged in the complaint show that Onilea Neal was given copies of inspection reports during her dealings with FmHA and Home Marketing. Miss Neal relied upon FmHA to supervise and inspect the construction of her home to make sure it was built right. The inspection reports themselves were merely *pro forma* and were incidental to FmHA's duty to supervise and inspect construction of Miss Neal's home with due care. The duty owed by FmHA could have been discharged without any inspection reports or any communication to Onilea Neal.

Finally, the government asserts that Congress created an exclusive remedy to correct defects in homes constructed under the rural housing program. 42 U.S.C. § 1479(c). (Pet. Br. 32) But nothing within 42 U.S.C. § 1479(c) precludes the right of a Section 502 borrower to claim relief under the Federal Tort Claims Act.[32] The fact that Congress provides an administrative compensation system does not prevent a FmHA borrower from bringing suit under the Federal Tort Claims Act.

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[32] The cases of *Laird* v. *Nelms*, 406 U.S. 797 (1972) and *Potnick* v. *United States*, 356 F.Supp. 395 (N.D.Miss. 1973) cited by the government (Pet.Br. 32) are inapposite. The plaintiff in *Laird* sought to recover damages which resulted from sonic booms by air force aircraft. The Court found that the plaintiff failed to show negligence and that the Federal Tort Claims Act did not waive immunity of the United States on claims based upon the theory of strict liability. The plaintiff in *Potnick* did not bring suit under the Federal Tort Claims Act.

See, e.g., United States v. *Muniz*, 374 U.S. 150 (1963); *United States* v. *Brown*, 348 U.S. 110 (1954). Absent a clear expression by Congress to make 42 U.S.C. § 1479(c) an exclusive remedy for damages suffered by Section 502 borrowers, one cannot be inferred.[33] *See United States* v. *Brown*, 348 U.S. at 112-113; *Brooks* v. *United States*, 337 U.S. 49, 53 (1949).

The legislative history of 42 U.S.C. § 1479(c) does not support any inference that Congress intended the FmHA compensation program to be an exclusive remedy. The House Report on the 1977 amendments to Title V of the 1949 Housing Act demonstrates that Congress expected FmHA to prevent construction defects in the Section 502 rural housing loan program by inspections and supervision.

> Complaints concerning shoddy construction in some FmHA homes and the inability of FmHA to correct the situation after the fact have come to your committee's attention. Most, if not all, of these instances of shoddy construction could have been avoided with proper inspection procedures and appropriate contractual arrangements (such as escrow agreements) with builders. Your committee expects the Secretary to put much greater emphasis on such administrative safeguards so that, as a result, the authority provided in this section [509(c)] will seldom have to be used.

H. Rep. No. 95-236, 95th Cong., 1st Sess. 27-28 (1977). House Report No. 95-236 gives no indication that Congress con-

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[33] In *Summers* v. *United States*, 510 F.2d 123 (8th Cir. 1975), *aff'g Cason* v. *United States*, 381 F. Supp. 1362 (W.D.Mo. 1974), *cert. denied*, 423 U.S. 851 (1975), the circuit court affirmed the district court's dismissal of the plaintiff's claim for damages under the Federal Tort Claims Act since the claim was based upon misrepresentation. 381 F.Supp. at 1367. Since the plaintiffs could not maintain a claim for misrepresentation against the government, the only remedy available was through the HUD administrative compensation program, 12 U.S.C. § 1735b(b). *Summers* is restricted to its facts and cannot be construed to infer that 42 U.S.C. § 1479(c) is an exclusive remedy absent clear Congressional expression to do so.

sidered *Neustadt* when it enacted Section 509(c) (42 U.S.C. § 1479(c)), or that it intended Section 509(c) to be an exclusive remedy.[34]

The government's analogy between Section 509(c) (42 U.S.C. § 1479(c)) and the legislative history of 12 U.S.C. § 1735b(b) does not support its claim of exclusivity. Although 12 U.S.C. § 1735b(b) may not have been intended to enlarge rights under the Federal Tort Claims Act, neither did it expressly diminish those rights.

Furthermore, the remedy provided under Section 509(c) is inadequate. Section 509(c) simply authorizes—does not require—FmHA to make expenditures where the statutory conditions for them are met. It does not require that the expenditures be made promptly or within a specified time limit.[35] It bars judicial review of the determinations which are being made by the same agency accused of negligently allowing substandard housing to be constructed. Section 509(c) does not require FmHA to take all necessary steps to notify FmHA borrowers of the availability of such relief. Expenditures are limited to correct "structural" defects which are discovered and for which claims are presented within 18 months after financial assistance is rendered.[36]

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[34] House Report No. 95-236 reinforces the conclusion that Congress intended the inspection and supervision of construction by FmHA to benefit the borrower by preventing "shoddy construction."

[35] Onilea Neal waited through 24 months and two winters before FmHA agreed to make expenditures to repair her heating system. See n. 8, *supra*.

[36] Not only does the compensation program fail to address the problem of serious defects which, though costly and dangerous, are not "structural," but its time limit bars many genuine claims discovered later. In Miss Neal's case, two serious defects in her home (lack of exterior sheathing and lack of anchoring to the foundation) were not discovered—and could not reasonably have been discovered—until other repairs were made. See n. 8, *supra*.

The court of appeals' opinion is consistent with a plain reading of statutes, regulations and legislative history concerning the FmHA Section 502 rural housing loan program. It carefully considered and analyzed the holding in *United States* v. *Neustadt*, 366 U.S. 696 (1961) in light of the complaint filed by Onilea Neal. (Pet. App. 14a-18a) Based upon the allegations and facts presented, the court of appeals reached the inescapable conclusion that Miss Neal had sufficiently alleged a claim for negligence and was entitled to her day in court.

In allowing Miss Neal to proceed with her complaint, the court of appeals did not, of course, find that she was entitled to relief. It held only that her complaint alleged a degree of incompetence and negligence which gives rise to a claim for relief under the Federal Tort Claims Act, and that she was entitled to an opportunity to prove that degree of negligence. "What relief, if any, could be given and how far it could go it is not yet time to discuss." *Hart* v. *B. F. Keith Vaudeville Exchange*, 262 U.S. 271, 274 (1923).

However, it is important to recognize that, if the court of appeals' ruling stands, and Miss Neal were to prevail after an ultimate trial on the remaining issues, FmHA could face little, if any, actual liability. In this case, as in most cases which would arise under Section 502, FmHA stands as a joint tortfeasor with the contractor. FmHA has the opportunity to cross-claim against the contractor and seek to avoid total liability. FmHA can also claim a set-off at trial for the costs of repairs which it has made. 28 U.S.C. § 1346(c).

The availability of claims against contractors and setoffs, and FmHA's ability to protect itself through a bond or escrow account, makes FmHA's fear of vast financial liability unfounded. (Pet. Br. 27-28). By working with established contractors which are reputable and solvent (which would seem to be required under the Act), by bonding requirements, or by escrow arrangements, the United States would not be exposed to new or costly payments to its damaged beneficiaries. If this case has any impact on FmHA, it would be to encourage more

careful selection of contractors and the exercise of due care in supervising and inspecting construction.

CONCLUSION

For these reasons, the judgment of the court of appeals should be affirmed.

Respectfully submitted,

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Petitioner's Reply Brief

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No. 81-1494

In the Supreme Court of the United States

OCTOBER TERM, 1982

JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET AL.,
PETITIONERS

v.

ONILEA NEAL

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

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1. In *United States* v. *Neustadt*, 366 U.S. 696 (1961), this Court decided a case virtually identical to this one. In *Neustadt*, the Court held first, that a claim that a government employee has negligently inspected a dwelling is one arising out of "misrepresentation," within the meaning of the exception to the Tort Claims Act in 28 U.S.C. 2680(h) (366 U.S. 706-708) and second, that Congress did not clearly express any intent in the inspection provisions of the National Housing Act of 1934, 12 U.S.C.

(& Supp. V) 1701 *et seq.*, to limit or suspend the misrepresentation exception (366 U.S. 708-710). Respondent and Amicus Curiae National Housing Law Project confuse the two prongs of *Neustadt* and argue that because the National Housing Act of 1934 is different from the Housing Act of 1949, the allegedly negligent inspection of respondent's house by a FmHA employee gives rise to a claim for something other than misrepresentation. *Neustadt* makes plain, however, that a suit based on the conveyance of misinformation because of a negligent inspection of a house, regardless of the statutory scheme that gives rise to the inspection, is a claim arising out of misrepresentation barred by Section 2680(h). Thus, regardless of the "specific duty" owed by the government (366 U.S. at 706), the inspection and reporting process is precisely what Congress excluded from liability under the Tort Claims Act.[1]

2. Respondent (Br. 6, 12, 32, 38, 42) and amicus (Br. 12, 38-39) attempt to avoid having respondent's claim characterized as one for misrepresentation by repeatedly emphasizing that the FmHA's "Record of Advances" lists September 30, 1977, as the day when the final disbursement of funds to respondent

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[1] Respondent may be arguing that if the government has some duty to respond to the discovered defect by action, rather than words, then her claim is not one for misrepresentation. As we indicated in our opening brief (Br. 19 n.10), this was precisely the argument made by the Neustadts and rejected by this Court in 1961. Moreover, respondent's argument is inconsistent with the broad language in Section 2680(h) referring to claims "arising out of" misrepresentation. Of course, the Court need not decide this issue since it is plain that the FmHA owed no duty to respondent based on the inspection, except perhaps to disclose any discovered defects.

took place. Both point out that the final inspection occurred on October 3, 1977, and argue that since the funds were disbursed prior to the final inspection respondent could not have relied upon the inspection report and therefore could not have asserted a claim for misrepresentation. There are two problems with this contention, which is made here for the first time in this lawsuit. First, respondent's claim regarding the date of the disbursement is inaccurate, which no doubt explains why it has never been presented previously. The check was prepared three days prior to the final inspection and the disbursement was noted as of that date, but the check was not actually given to respondent until *after* the final inspection. And it was not until after the October 3 inspection that respondent endorsed the check over to the contractor. Thus, as a matter of fact, respondent could have relied upon the report as a basis for purchasing her house.

In any event, respondent's factual assertion regarding the date of the check does not affect our submission. Either respondent's claim is one for misrepresentation based on the report or she has no claim against the United States at all. Respondent's attempt to restate the facts to deny reliance on the FmHA's misrepresentation illustrates one of the anomalies, noted in our opening brief (Br. 19), created by the misrepresentation exception to the FTCA —plaintiffs assume positions directly contrary to ones they would in a normal tort suit not involving the United States as defendant. The applicability of the misrepresentation exception must, of course, be determined by reference to the true nature of respondent's claim, not the version proffered to avoid the strictures of Section 2680(h). Thus, whether respondent contends that she actually relied upon the

FmHA inspection report is of no significance; the essence of her claim still "aris[es] out of * * * misrepresentation."

3. Since her claim is plainly one for misrepresentation, in order to prevail under *Neustadt* respondent must show that Congress clearly intended to suspend or supersede the operation of the misrepresentation exception when it enacted the rural housing loan program in the Housing Act of 1949, 42 U.S.C. (& Supp. IV) 1476. But respondent has not supplied any substantial basis for distinguishing the 1949 Act from the 1934 Act involved in *Neustadt* in this respect. Both Acts created inspection programs designed primarily to protect the government.[2] Neither statute even hints that the inspection process was designed to create some duty not within the ambit of the misrepresentation exception.[3]

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[2] Amicus disputes FmHA's reading of its statute (Br. 9), but can cite to nothing in the statute, regulations or legislative history to support its claim. Instead, amicus relies upon the same deposition testimony of a builder cited by respondent, which is neither supportive of respondent's position nor authoritative. Amicus also refers to (Br. 41-42) an internal memorandum from an attorney in the Department of Agriculture to the FmHA Administrator suggesting nondisbursal as a possible course of action. That memorandum, which we have reproduced in full (App., *infra*, 1a), actually supports our primary submission in this case. The memorandum, which was written in 1976, states that "the Government makes inspections for its own benefit and not for the benefit of the borrower" (*ibid.*). Although the writer of the memorandum does propose that the FmHA institute a practice of refusing to disburse funds in selected cases involving construction defects, there is no suggestion that that option is mandated by the statute.

[3] Respondent maintains that the FmHA could have withheld the proceeds of the loan from her, if it had discovered

Amicus attempts to portray the FmHA as a surrogate purchaser under the rural housing loan program in Section 502 of the 1949 Housing Act and the loan recipient as a helpless bystander who is expected to rely completely on the county supervisor to take care of every detail of the transaction (see Amicus Br. 22-25). The very regulations it quotes so extensively indicate clearly, however, that the FmHA's role is primarily as an advisor to the borrower. Thus, the FmHA does no more than recommend a number of contractors and leaves it to the borrower to initiate the negotiations for the purchase of a house. Under 7 C.F.R. 1802.65(a)(2) (1977) (Amicus Br. 23), the supervisor should be prepared with "information" to assist the borrower, and under 7 C.F.R. 1804.3(f)(2)(iii) (1977) (Amicus Br. 24) the supervisor should "advise" the applicant

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the defects. By like reasoning, it could also have hired a new contractor to rebuild the house or purchased the defective house and had a new one built for respondent. Indeed, the supervisor could personally have bought her a new heat pump. The problem is that although there are a number of gratuitous responses the FmHA *could* adopt when it discovers a defect, none of them is required by the statute or regulations, because the inspection is designed primarily to protect the government, not the borrower.

Amicus also argues (Br. 40-41) that, in addition to the alleged duty to refuse to release funds to respondent if there are defects, the FmHA could have required the contractor to provide a surety bond. But in a situation such as the one involved here, where the contractor is a going concern that previously has done satisfactory work, there would be no reason to require the posting of a bond. See 7 C.F.R. 1804.4 (d)(2)(i)(b) (1977). What respondent and amicus simply refuse to acknowledge is that the true wrongdoer, and the true defendant to respondent's claim, is the contractor—against whom respondent still has a law suit pending.

with regard to plans and specifications. The provision goes on to require the supervisor to "advise" the borrower regarding other sources of governmental information, 7 C.F.R. 1804.3(f)(2)(iv) (1977), and to "offer suggestions" that will assist the borrower with regard to his planned housing, 7 C.F.R. 1804.3 (f)(2)(vi) (1977) (Amicus Br. 24-25).

Thus, the regulations adopted pursuant to the 1949 Act do not describe the supervisor as the person who makes the crucial decisions and thereby guarantees a house free of defects; instead, the supervisor merely provides advice and suggestions while the house is being constructed and helps negotiate disputes between the contractor and borrower if the housing that is purchased turns out to be unsatisfactory. It is fully consistent with this scheme for the FmHA simply to advise the borrower of defective conditions it discovers that do not affect the structural integrity of the house.[4] What the Court said in *Neustadt* is equally applicable here: "Never once was it even intimated that, by an [FmHA] appraisal, the Government would, in any sense, represent or guarantee to the purchaser that he was receiving a certain value for his money." 366 U.S. at 709.

Nor is respondent's claim (Br. 13 n.14) supported by the absence of a specific requirement that the FmHA

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[4] Amicus also relies (Br. 26-27) on the contract as support for its claim that the FmHA asserts absolute control over the purchase of a house. All of the contractual provisions cited, however, are included to protect the government's security interest. In this regard, the court of appeals expressly held (Pet. App. 11a), and respondent has never challenged the finding, that the contract created no obligation running to respondent to supervise construction or to inspect her house.

disclose the inspection report to the borrower. First, in practice, the borrower accompanies the inspector and signs the final inspection report, 7 C.F.R. 1804.4(g)(3)(iv) (1977); indeed, respondent did that in this case. Disclosure of defects, if uncovered, would occur at that time. Second, the absence of a specific requirement to disclose defects to the borrower is fully consistent with what we claim is the primary purpose of the inspection, *i.e.*, to protect the government's security interest. Thus, the inspection report is designed to inform the agency as to whether the house has major defects that might reduce its value, and there is no reason to provide the borrower with a copy.[5]

4. Relying upon *United States* v. *Muniz*, 374 U.S. 150 (1963), and *United States* v. *Brown*, 348 U.S. 110 (1954), both respondent (Br. 42-43) and amicus (Br. 46) argue that the availability of relief under 42 U.S.C. (Supp. IV) 1479(c) ought not to be viewed as precluding Tort Claims Act recovery for the FmHA's allegedly negligent inspections. The fundamental difference between this case and *Muniz* and *Brown*

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[5] Relying on generalized statements in the regulations and the legislative history about the beneficent purposes of the rural home loan program, amicus argues (Br. 15-19) that the inspection program is designed to benefit the borrower. Amicus does not deny, however, that there are explicit references in both the legislative history and the regulations which indicate that the purpose of the inspection itself is to protect the government's security interest, because the nature of the inspection is dependent on the size of the loan. We have never denied that the borrower would be a beneficiary of the inspection process, just as the borrowers in the FHA program involved in *Neustadt* (366 U.S. at 710 n.24) were benefited by the FHA inspections. But being a beneficiary of an inspection is legally insufficient under *Neustadt* to warrant disregarding the misrepresentation exception.

(other than the clear applicability of 28 U.S.C. 2680(h) here) is that Section 1479(c) was enacted after the Tort Claims Act and after this Court's decision in *Neustadt* and was passed expressly to provide a partial remedy that would otherwise be barred by the misrepresentation exception. Thus, unlike in *Muniz* and *Brown*, we are not left to guess how to accommodate the two compensation schemes. Section 1479(c) is the only remedy Congress anticipated would be available to a loan recipient in respondent's position. The section thus reflects Congress' understanding that the FmHA loan program's provision for inspections is indistinguishable in its purpose and effect from that in the 1934 Housing Act involved in *Neustadt*,[6] and respondent's and amicus' complaint about the adequacy of Section 1479(c) relief is addressed to the wrong branch of government. Moreover, the most likely reason why Congress limited the scope of federal administrative relief is because the real defendant in these cases should be the contractor or builder, whose negligence caused the defect in the house. Thus, a governmental remedy simply was not necessary for the vast majority of cases.

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[6] If respondent's interpretation of the 1949 Housing Act were correct, then Section 1479(c) would be superfluous. The FTCA includes an existing administrative mechanism for obtaining relief from an agency without having to litigate a tort claim. 28 U.S.C. 2672, 2675(a). If negligent FmHA inspections give rise to liability under the Tort Claims Act, then such claims would necessarily have to be filed in the first instance under the administrative process in the FTCA. No plaintiff would ever need to file for relief with the FmHA under Section 1479(c). The Court should not adopt a construction of the 1949 Act that would render subsequent legislation superfluous. See *United States* v. *Greathouse*, 166 U.S. 601, 604-605 (1897); 1A Sands, *Sutherland Statutory Construction* §§ 23.09-23.10 (rev. ed. 1972).

5. In sum, this case is legally indistinguishable from the FHA program involved in *Neustadt*. Congress has not seen fit to overrule *Neustadt* in the 20 years since it was decided; to the contrary, Congress established an administrative compensation scheme on the express understanding that persons in respondent's position could not sue the United States under the FTCA. See *Lorillard* v. *Pons*, 434 U.S. 575, 580-581 (1978). In these circumstances, it would be inappropriate for this Court to construe the Housing Act of 1949 to limit the broad exception to the waiver of sovereign immunity contained in 28 U.S.C. 2680(h) and to subject the United States to potentially massive, and wholly unanticipated, damages liability.

For the foregoing reasons, and the reasons stated in our opening brief, it is respectfully submitted that the judgment of the court of appeals should be reversed.

REX E. LEE
Solicitor General

JANUARY 1983

APPENDIX

Dec. 9, 1976

SUBJECT: Construction Defect Cases

To: Frank B. Elliott
Administrator
Farmers Home Administration

Attached is an example of a construction defect case. This type of case is occurring with increasing frequency.

You may be interested in reading the nature of the defects of which this plaintiff, Augusta Parker, complains. They are set forth on page 5 and are obviously rather serious. These particular allegations are probably somewhat exaggerated but some serious defects no doubt exist.

As we have previously explained the law to you, the Government makes inspections for its own benefit and not for the benefit of the borrower. To date, the courts have not held that the Government owes a duty to properly inspect to the borrower. With the number of these cases being brought, eventually some court is going to enter an order adverse to the Government.

It would appear that FmHA should place more emphasis on proper inspection and corrective action that should be pursued where defects are found. For example, the most obvious action where defects are noted is the nondisbursal of remaining loan funds to the contractor until all defects are corrected.

We realize that most county supervisors are carrying an extremely heavy workload, but the inspection re-

quirement is one imposed by statute which must be met.

/s/ James V. Loughran, Jr.
JAMES V. LOUGHRAN, JR.
Director
Community Development Division

Attachment

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Amicus Brief

1

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No. 81-1494

IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1982

JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET. AL.,
PETITIONERS

v.

ONILEA NEAL

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE AMICUS CURIAE

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JOHN R. BLOCK, SECRETARY OF AGRICULTURE, ET. AL.,

PETITIONERS

v.

ONILEA NEAL

BRIEF FOR THE AMICUS CURIAE

I. INTEREST OF AMICUS[1]

This brief is in support of Appellee Onilea Neal. It is submitted on behalf of Mitchell Park who is the appellee in Park et al. v. United States, 517 F.Supp. 970, (D.C. Or. 1981) [Appellate No. 81-3524] currently on appeal in the United States Court of Appeals for the Ninth Circuit. The issues in that case are substantially

1. The parties have consented to the filing of this brief and their letters of consent have been filed with the Clerk of the Court pursuant to Rule 36(2) of the Rules of this Court.

the same as those presented in this action and as a consequence, the Court's decision will necessarily affect the interests of the Parks.

II. SUMMARY OF ARGUMENT

Amicus argues that the affirmative undertaking of the government in providing home buyers technical assistance prior to, during, and after the construction of homes financed under the Housing Act of 1949, 42 U.S.C. §1471 et seq., creates a duty to perform operational tasks for the benefit of borrowers, which if not properly performed can create governmental liability pursuant to the Federal Tort Claims Act, 28 U.S.C. §2674 et seq (F.T.C.A.) They also argue that the misrepresentation exception, 28 U.S.C. §2680(h), does not apply because the government undertaking involves the performance of operative tasks.

III. ARGUMENT

A. INTRODUCTION

The FmHA program creates a special relationship between the county supervisor and the borrower which does not exist in other federal programs, specifically programs funded pursuant to the Federal Housing Act. The relationship is characterized by a range of affirmative undertakings on the part of the government agency which exerts a great deal of control over the financial transactions, site preparation and building construction, all of which assumes and encourages the borrower's reliance on the FmHA agent's technical expertise. As a consequence, the FmHA program confers a

duty of care on the part of the government which if performed negligently gives rise to liability under the F.T.C.A.

The facts in the case of Mr. and Mrs. Park, on whose behalf this brief is filed, demonstrate the extent of involvement of the federal government in the construction and planning of homes pursuant to the FmHA §502 program. The FmHA supervisor first, convinced the Parks to purchase a new home rather than an older home, second, they referred the Parks to a list of approved builders, third, they inspected the home on three separate occasions, fourth, they released the payments to be made to the builder and finally, they were deeply involved in attempts to solve post-occupancy problems.

B. The Initial Meeting Between the County Supervisor and the Parks Was a Governmental Undertaking Which Created a Cognizable Duty.

In early 1976, the Parks visited the FmHA office in St. Helens, Oregon, where they met with James O. Dias, the FmHA County Supervisor. Mr. and Mrs. Park had not owned, or been involved in the construction of a home prior to seeking assistance from FmHA. Although the Parks' had contemplated buying an existing home, not a newly constructed one, they were advised by Mr. Dias against purchasing an existing home and acting on his advice decided to purchase a new home.

It was during this meeting that the Parks' came to perceive "the role of the FmHA office as an overseer and inspector of the house they would be purchasing." Park v. U.S., supra at 976. This belief

was founded upon the representations of Mr. Dias and FmHA documents which stated, among other things, that (a) the government would not allow occupancy of their new home until final inspection had been completed; (b) FmHA would assist them in resolving warranty complaints with the builder should they arise; (c) the new home would be periodically inspected to assure compliance with FmHA regulations; and (d) the new home would have to be built pursuant to stringent construction standards. Id. at 972.

C. The Referral of the Parks to a Specific Builder, the Inspections of the House, and the Release of Monies, Were Operational Tasks Which Cannot Be Characterized as Misrepresentations

The Parks were unable to find a builder on their own despite several contacts with local builders from an approved FmHA list. As a result, Mrs. Park obtained from FmHA the names of contractors that had previously built FmHA homes and were "approved." Id. at 972. The builder eventually chosen, Mr. Steinke, was approved by FmHA and furthermore was referred to by FmHA employees as "one of their best" contractors. In essence FmHA chose the builder for the inexperienced Parks.

The lower court in Park, supra, found the following facts;

> Dias gave her the impression that the construction of the house would be observed and inspected and that this would be done according to the regulations and requirements of the agency.

> ...Dias told him (Mr. Park) that the inspections would assure that everything take place according to FmHA regulations. Park perceived the role of FmHA as a supervisor over the builder. Park at 976.

Dias, in fact, undertook several inspections of the site. Acting in his capacity as FmHA supervisor he personally inspected the site and found it to be suitable. Park at 972. On March 8, 1976, he issued a conditional commitment for FmHA financing conditioned on compliance with applicable regulations. Id.

At the time Dias first viewed the property, a rock ledge approximately four feet high was present on the site. Id. at 972. Upon commencement of construction, Steinke undertook substantial excavation of the site and in the process created a twenty-five foot high vertical rock cliff running east to west through the property. Id. at 972. The Parks questioned Steinke about the detrimental effect of the rock cliff on the house and property. Steinke assured them there was no cause for concern. Id.

During the construction, James Dias, acting in his capacity as FmHA County Supervisor, on three separate occasions certified that he had inspected and approved the site and home. Final approval was given on June 28, 1976. Id.

On June 14, 1976, the Secretary of Agriculture, acting through Dias, approved the Parks' application for a Section 502 loan and a contract was entered into with the Parks to furnish a loan in the amount of $25,000 for the purchase of the Steinke

home. Id. On that date, Dias, as the "approving official", certified that all laws, regulations, determinations and certifications required by FmHA as prerequisites for the loan had been complied with by Steinke and the Parks. Id. On June 28, 1976, the Parks executed a Promissory Note and a Real Estate Deed of Trust, which incorporated all existing and future FmHA regulations. Id. During the period of ownership all house payments were made directly to FmHA. Id. On June 29, 1976, Steinke executed a "Builder's Warranty" to the Parks, as required by FmHA. Id. at 972, 973.

D. The Post-Occupancy Problems of the Parks.

Shortly after the Parks occupied the house on July 2, 1976, they observed numerous defects in the site preparation and construction of the home, including the excavated rock wall immediately adjacent to the south side of the house. Id. at 973. The basalt cliff was unstable and crumbled, depositing large pieces of rock on the roof and against the side of the house. Id. Falling rocks damaged the siding and windows of the house and presented a severe danger to the Parks' physical and emotional well-being. Id.

The Parks complained to the builder and to FmHA on August 3, 1976. Id. They were advised by FmHA employees to send written notice of the defects to the builder, which they did. Id. On October 8, 1976, Mitchell Park sought assistance from the Chief of Rural Housing at the State FmHA office, who recommended he contact the builder, sell the house or seek legal advice. Id.

In August and October 1976, Mitchell Park was advised by FmHA agents to build a retaining wall, using the rock debris to create a catch basin for falling rocks. Id. Mr. Park attempted to follow these recommendations, believing that it was his duty as an FmHA borrower to protect the house and property. Id.

During the period July, 1976 through August, 1978, the Parks' numerous requests for assistance from FmHA in requiring Steinke to repair the defects were without success. Id. On several occasions, Steinke, when asked about the safety of the rock cliff, informed the Parks that FmHA's inspections and approval of the home and site indicated to him that all building code and regulatory requirements had been met. Id.

In November, 1977 the matter was referred to the FmHA State Office, which sent an FmHA Construction Analyst, Walter Naysmith, to visit the site. Id. Naysmith subsequently filed a report stating that the rock cliff was "extremely unstable" and posed an "extreme hazard" to the occupants of the house. Id. The Parks were not informed of these findings and first became aware of this report during the course of discovery in June, 1978. Id. at 974.

IV. CONCLUSION

Specific facts are especially relevant to the issue to be decided in Neal, supra as well as Park, supra because the actual relationship between the parties defines the nature of any undertaking and subsequent liability. The

thrust of the government's argument in both Neal and Park has been that the actions taken by FmHA involve cursory inspections designed to protect the government's security interest. Failure to convey the results of those inspections are mere misrepresentations under the reasoning of United States v. Neustadt, 366 U.S. 696 (U.S. 1961). The facts in Park reflect a radically different undertaking on the part of the government. The government agents were intergrally involved with every important decision the Parks' made concerning their home purchase, beginning with the decision to buy a new house rather than purchase an existing home, to the actual selection of the builder, to the inspection of the home for defects and finally ending in the attempted solution of the post occupancy problems. In addition, the government as the direct lender was in the position to withhold payments until construction defects were remedied. The government undertaking involved the performance of operative tasks which created liability if they were negligently performed.

The Court is not being asked to make new law. An examination of the facts in Park (and other FTCA claims) underscores the wisdom of making determinations on a case-by-case basis. Within the framework of the FmHA statutory scheme it is possible for the government to undertake activities that form the basis for governmental liability. Whether or not particular actions are barred by the misrepresentation exclusion to the F.T.C.A. is a factual question which can be decided on a case-by-case basis.

Amicus Brief

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versus

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On Writ of Certiorari to the
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for the Sixth Circuit

BRIEF OF AMICUS CURIAE IN SUPPORT OF RESPONDENT

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STATEMENT OF INTEREST OF AMICUS CURIAE

The National Housing Law Project (Project hereinafter) has an interest in the case sub judice arising from its role as a national support and backup center to approximately 265 local Legal Sevices projects throughout the country. The Project is a California nonprofit corporation primarily funded by a contract with the Legal Services Corporation. The chief function of the Project is to serve as a resource for the more than 5,000 local Legal Services attorneys throughout the country. These attorneys advise and represent approximately 1.5 million low-income clients annually, and about 20 percent of these cases involve housing issues. Respondent in the instant case is represented by staff attorneys for the Rural Legal Services of Tennessee, located in Oak Ridge, Tennessee.

Project staff attorneys assist neighborhood Legal Services lawyers in helping their low-income clients in the subject matter areas of federally subsidized housing programs, private landlord-tenant relations, public housing, urban renewal, community economic development, low-income housing production and preservation and a myriad of other matters relating to housing, tenants' rights and urban and rural affairs. In addition to providing assistance in individual cases, the Project is dedicated to attempting to further the development of the law in the area of housing towards an increasing recognition of the rights and needs of low-income tenants and homeowners in the United States.

The Project fully supports the arguments presented by Respondent in her brief.

STATEMENT

Ms. Onilea Neal is a low-income person lacking experience in housing construction. She obtained a Farmers Home Administration (FmHA) loan for the construction of a home in Roane County, a rural area of Tennessee. Ms. Neal located a contractor with the assistance of FmHA and, with its guidance, entered into a construction contract. Thereafter she justifiably relied upon the FmHA to carefully inspect and supervise the construction of her home. FmHA, however, was negligent in its undertaking and as a result Ms. Neal suffered substantial damages (J.A. 3-20).

The FmHA, pursuant to Title V of the Housing Act of 1949, 42 U.S.C. § 1471 et

seq.,[1] operates a unique program of supervised credit for low- and moderate-income rural residents in need of decent, safe and sanitary housing. Its program has two components: direct[2] unsubsidized and subsidized loans for the construction, acquisition or rehabilitation of housing, 42 U.S.C. §§ 1472 and 1490a(a)(1)(A); and technical services such as building plans, specifications, construction supervision and inspection, 42 U.S.C. § 1476. The FmHA single-family homeownership program is known as the Section 502 program.

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1 Unless noted, all citations to statutes and regulations are those that were in effect at the time of Ms. Neal's loan.

2 FmHA's authority is to make direct or insured loans. 42 U.S.C. § 1472. Its insured loans are nonetheless direct in the sense that the FmHA itself makes the loan to the borrower.

Each year FmHA makes about 100,000 Section 502 loans. USDA, FmHA, Housing Program Statistics, 1976-1977 Supplement, 1 (1978). They are made to persons whose incomes do not exceed FmHA limits for families with moderate incomes and who are unable to obtain credit from other sources. See 42 U.S.C. §§ 1471 and 1472. At least 60 percent of FmHA loans must be to persons with low incomes. 42 U.S.C. (& Supp. IV) § 1487(o)(1).[3] At the time of respondent Ms. Neal's loan, a low-income person was defined as an individual residing in the continental United States with an annual adjusted family income under $10,000. 7 C.F.R. Part 1822,

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[3] Prior to 1979, this requirement was included in the annual appropriations for FmHA. See e.g., Agriculture and Related Agencies Programs -- Appropriations, Pub. L. No. 95-97, Title II, 91 Stat. 810, 818 (1977).

Subpart A, Ex. C (1977). Almost all the loans made to low-income families are subsidized by the FmHA Interest Credit Program. 42 U.S.C.A. § 1490a(a)(1)(A). See USDA, FmHA, Housing Program Statistics, 1976-1977 Supplement, 2 (1978).

FmHA borrowers are generally poorly educated, lack previous homeownership experience and have limited financial resources. More than 85 percent of them have less than a high school education and over 17 percent have less than eight years of schooling. Spurlock, Mortgaged Rural Homes -- Characteristics of Housing Units and Occupants 18 (Nov. 1979) (Economic Dev. Div., Economics Statistics, and Coop. Serv., USDA, Rural Dev. Report No. 17). Nearly 81 percent of FmHA borrowers were renters prior to receiving FmHA loans. Id. 11. Over 82 percent have household incomes under $15,000 and nearly 47 percent have annual household

incomes of less than $10,000. Id. 15. Between 15 and 25 percent of FmHA borrowers are recipients of Social Security or welfare assistance. Id. 21. Most borrowers who are "low-income" have less than $5,000 in net assets.[4] In short, most FmHA borrowers do not have the education or experience to adequately inspect or supervise construction of their homes and do not have the financial resources to hire competent professionals to do it for them.

Under the Section 502 program, new construction is carried out by way of a "conditional commitment," the "borrower method" or "contract method." Conditional commitments are typically used by builders who construct houses subject to

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[4] See 7 C.F.R. Part 1822, Subpart A, Ex. E, ¶ 3(a)(1)(ii) (1977).

FmHA specifications and approvals and subsequently sell these homes to FmHA-qualified individuals. See 7 C.F.R. § 1822.301 et seq. (1977). The borrower method is used by individuals who are competent to purchase materials, contract for and supervise construction or are themselves capable of undertaking portions of, or all, the construction. See 7 C.F.R. § 1804.4(e) (1977). The contract method is used by individuals who are determined eligible for an FmHA loan and who, with FmHA assistance, then contract for the construction of the home. 7 C.F.R. § 1804.4(d) (1977). Individuals who use the contract method often do not know how to plan for and construct a home. They look to an FmHA official to provide them direction and supervision. See USDA, Rural Housing Survey and an Analysis of Rural Housing Programs 18

(March 1979) (Survey of the Equal Opportunity Staff of the Farmers Home Administration conducted jointly with USDA's Office of Equal Opportunity). Respondent Ms. Neal used the contract method in constructing her home.

FmHA county supervisors, or their assistants, are authorized and required to provide borrowers with technical services and supervision. 7 C.F.R. §§ 1822.7(a) and 1822.9 (1977). This usually includes an explanation of FmHA's design criteria and requirements and may include the provision of plans and specifications. 7 C.F.R. § 1804.3(f)(2) (1977). Often FmHA staff will steer eligible applicants to one or more FmHA-approved builders. The borrower, with the advice of FmHA, selects a builder and FmHA provides the borrower with all necessary contracts, forms and services necessary to close the loan and commence

construction. See 7 C.F.R. §§ 1822.9 and 1822.12 (1977). If the contract between the contractor and the borrower contemplates payments during construction, the proceeds of the FmHA loan are disbursed into a supervised bank account. 7 C.F.R. § 1803.2 (1977). A supervised account requires the signature of the borrower and the countersignature of the county supervisor for withdrawals. 7 C.F.R. § 1803.5 (1977).

During construction, FmHA conducts inspections and authorizes payments depending on the work completed and materials in place. 7 C.F.R. § 1804.4(d)(7)(v) (1977). If the contractor has a surety bond, payments are made for up to 90 percent of the work in place; if not, payments are only authorized for up to 60 percent of the work in place. 7 C.F.R. § 1804.4(d)(7)(i)(c) (1977). Ms. Neal's contract called for

payments based on 60 percent of the work in place (J.A. 26-27). If any materials or work are unsatisfactory or not in accordance with plans and specifications, FmHA is authorized to reject it and withhold payments. See J.A. 26-27; C.A. App. 120-121.

After construction is complete, the contractor is required to provide the borrower with a warranty, 7 C.F.R. § 1804.4(d)(6)(i)(k) (1977), and any remaining construction disputes are resolved by FmHA, 7 C.F.R. § 1804.4(g)(5) (1977). In short, under the contract method of construction, FmHA is integrally involved in every step of the construction process.

SUMMARY OF ARGUMENT

Construction supervision and inspections are technical services provided by FmHA to its borrowers as part of a comprehensive loan program authorized by Congress and designed to provide low- and moderate-income rural residents an opportunity to construct and own decent, safe and sanitary housing. Proper supervision obligates FmHA employees to use a wide range of services to assist its borrowers under a variety of circumstances. It may include assistance in locating a contractor, preparing plans and specifications and completing and executing construction contracts. It also includes proper inspection and supervision of construction.

It is well recognized that when the government performs a service negligently it may be held liable for its negligence.

Indian Towing Co. v. United States, 350 U.S. 61 (1955). It is also recognized that if the government's negligence arises out of a misrepresentation, recovery of damages is barred by the "misrepresentation" exception to the Federal Tort Claims Act, 28 U.S.C. § 2680(h). United States v. Neustadt, 366 U.S. 696 (1961).

In an attempt to avoid liability for its negligent inspection and supervision of the construction of Ms. Neal's home, FmHA argues that it owed Ms. Neal no duty that gives rise to her claim of negligence and that her claim arises from a misrepresentation, namely, her reliance upon a negligently prepared inspection report.

In its argument, FmHA ignores crucial differences between its authority under the Housing Act of 1949, 42 U.S.C. § 1471 et seq., and that of the Federal

Housing Administration (FHA), considered by this Court in Neustadt, under the Housing Act of 1934. 12 U.S.C. § 1701 et seq. Contrary to the facts, FmHA wrongly characterizes Ms. Neal's case as arising out of FmHA's failure to communicate undetected defects in its inspection report.

This case is not controlled by Neustadt. Ms. Neal has not alleged a misrepresentation on the part of FmHA and the facts show that Ms. Neal could not have relied on FmHA's inspection report.

Ms. Neal has alleged a simple case of negligence which is controlled by Indian Towing Co.. Her ability to recover under the Federal Tort Claims Act is not inconsistent with relief available under 42 U.S.C §1479(c). She should therefore be allowed to proceed with her case.

ARGUMENT

A SUIT ALLEGING FmHA'S NEGLIGENT SUPERVISION AND INSPECTION OF A HOME IS NOT BARRED BY THE MISREPRESENTATION EXCEPTION TO THE FEDERAL TORT CLAIMS ACT, 28 U.S.C. § 2680(h).

1. FmHA inspections and supervision are carried out pursuant to a statutory scheme intended to provide borrowers with decent, safe and sanitary housing.

FmHA, relying on United States v. Neustadt, 366 U.S. 696 (1961), argues strenuously that supervision and inspections conducted by it pursuant to Title V of the Housing Act of 1949, 42 U.S.C. § 1471 et seq., are primarily for the protection of the government's security interest (Pet. Br. 22-29). FmHA ignores

critical differences between its own inspection and supervision program and that carried out by the FHA under the National Housing Act of 1934. 12 U.S.C. § 1701 et seq. Those differences make it clear that FmHA's inspection and supervision program are for the benefit of the borrower.

Title V of the Housing Act of 1949 authorizes FmHA to make loans to low- and moderate-income rural residents for the purchase and construction of decent, safe and sanitary housing, 42 U.S.C. § 1472, and to provide them technical services, including supervision and inspection, to achieve the purposes of the legislation, namely, the provision of decent, safe and sanitary housing. 42 U.S.C. § 1476. Congress adopted Title V at the urging of the Department of Agriculture after it was informed that

farm families could not obtain mortgage credit, even when insured by the FHA, or adequate technical services to assure proper and economical construction of their homes. Hearings Before the Senate Committee on Banking and Currency on S.1592, 800-801, 79th Cong., 1st Sess. (1945); see S. Rep. No. 84, 81st Cong., 1st Sess. 25 (1949).[5]

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[5] What eventually became Title V of the Housing Act of 1949, 42 U.S.C. §§ 1471-1480, was first introduced in 1945 as part of S.1592, 79th Cong. S.1592 passed the Senate in 1946 but failed to pass the House. It was reintroduced as S.866 in 1947, amended and passed by the Senate, but died at the end of 1948 without reaching a vote of the House. It was reintroduced as S.1070 in 1949 and enacted that year. During the four years that Congress considered the Act, the Department of Agriculture worked closely with the Senate Committee in drafting Title V and vigorously advocated its adoption. See Hearings on S.866, Committee on Banking and Currency, House of Representatives, 80th Cong., 2d Sess., 315 (1948).

The 1949 Act, the Senate and House reports accompanying it, and, most importantly, FmHA's own regulations make it clear that the authority to provide technical services, including supervision and inspection, is intended to benefit FmHA borrowers. Section 506(a) of the Housing Act of 1949, 42 U.S.C. § 1476(a) provides, in part:

> Buildings and repairs constructed with funds advanced pursuant to this subchapter shall be supervised and inspected as required by the Secretary. In addition the Secretary is authorized to furnish . . . to any person, including a person eligible for financial assistance under this subchapter, without charge or at such charges as the Secretary may determine, technical services such as building plans, specifications, construction supervision and inspection, and advice and information regarding farm dwellings and other buildings. [Emphasis added.]

The Senate Report accompanying Title V of the 1949 Act states: "The bill also

contains an extremely necessary and desirable authorization which permits the expansion of technical services, such as plans, specifications, construction supervision and inspection, and advice and information in the Department of Agriculture. . . ." S. Rep. No. 84, 81st Cong., 1st Sess., 25 (1949). The House Report states:

> This section also authorizes the supervision and inspection of construction to the extent which may be found necessary for accomplishing the purposes of this title and for the preservation of the Government's security interest.

H.R. Rep. No. 590, 81st Cong., 1st Sess., 55-56 (1949).

From the statute, the Senate and House Reports it is clear that the purposes of FmHA's supervision and inspections are to ensure the provision of decent, safe and sanitary housing to rural residents; the protection of the

government's security interest; and the provision of technical assistance to borrowers. Of these, Congress and the Department of Agriculture considered the provision of technical services, including supervision and inspection, of vital importance. See Hearings on S.866, Committee on Banking and Currency, House of Representatives, 80th Cong., 2d Sess., 293 (1948). See also 95 Cong. Rec. 4615-4616 (1949) (remarks of Sen. Lucas); 95 Cong. Rec. 8143 (1949) (remarks of Cong. Buchanan).

FmHA regulations confirm the agency's obligation to assist borrowers by providing them with supervision, technical services such as building plans, specifications, construction supervision and inspection, and advice and information. The regulations state that the "primary objectives of supervision are to assist such families to . . . obtain decent,

safe and sanitary housing." 7 C.F.R. § 1802.2(b) (1977).[6]

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[6] FmHA relies on 7 C.F.R. § 1822.7(a) (1977) for the proposition that supervision is provided in order to protect the interests of the government and argues that this long-held interpretation by the agency should be accorded great deference (Pet. Br. 24-25). It omits critical elements of the regulation which, in full, states: "Supervision will be provided borrowers to the extent necessary to achieve the objectives of the loan and to protect the interests of the Government in accordance with Subpart A of Part 1802 of this Chapter." 7 C.F.R. § 1822.7(a) (1977). Subpart A of Part 1802, in turn, states that supervision and supervisory assistance "include the broad scope of management services available through the agency to families receiving or utilizing FmHA credit." 7 C.F.R. § 1802.1(b) (1977). It goes on to state that "all loans made by FmHA are designed to assist individual borrower families to attain specific objectives. Therefore, each borrower family will be provided the supervision necessary to achieve those objectives and to protect the financial interests of the Government." 7 C.F.R. § 1802.2(a) (1977) (emphasis added). In direct contradiction to FmHA's argument, the regulation next states that the "primary objectives of supervision are to assist such families to . . . obtain decent, safe and sanitary housing." 7 C.F.R. § 1802.2(b) (1977) (emphasis added).

The broad range of services encompassed in FmHA supervision includes planning, recordkeeping, supervisory visits, group supervision, timely guidance, annual analysis and credit counseling.[7] 7 C.F.R. § 1802.3 (1977). Supervision also extends to the disbursement of funds through the use of supervised bank accounts, 7 C.F.R. § 1803.2(f) (1977), to inspection of construction and to the planning and performance of development work. See 7 C.F.R. §§ 1804.2(d), 1804.3(f)(2) (1977).

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[7] FmHA supervisory regulations are applicable to both its housing and farm loans. Many of the regulations were originally adopted for its farm loan program but were later extended to cover its housing programs. In order to carry out effective supervision, county supervisors are instructed to select the supervisory method that will be most effective in helping each family. 7 C.F.R. § 1802.5(a) (1977).

FmHA regulations are both extensive and very explicit in the types of activities that county supervisors must perform in extending technical and supervisory services to borrowers. County supervisors are authorized to: guide borrowers in "planning for and making the best use of land, buildings . . . labor and skills" (7 C.F.R. § 1802.12(c) (1977)); assist borrowers in reviewing and evaluating their "nonagricultural operations to determine progress, problems and corrective action needed" (7 C.F.R. § 1802.32 (1977)).

When meeting with the borrower, the county supervisor is directed to "note the condition of the . . . home" (7 C.F.R. § 1802.63(b)(4)(iii) (1977)), and "[e]valuate the progress being made with respect to planned development" (7 C.F.R. § 1802.63(b)(4)(iv) (1977)).

If problems arise, the county supervisor "should assist the borrower family in obtaining the services of a competent specialist" (7 C.F.R. § 1802.63(b)(4)(v) (1977)). County supervisors are further directed to "[a]ssist the borrower family in making needed adjustments or revisions in their plans" (7 C.F.R. § 1802.63(b)(4)(vii) (1977)); to inspect the major purchases made with loan funds by the borrower" (7 C.F.R. § 1802.63(b)(4)(viii) (1977)) (emphasis added); and to "[c]onsider with the family the adequacy of property insurance and discuss any pending partial releases, subordination or leases affecting FmHA security property" (7 C.F.R. § 1802.63(b)(4)(ix) (1977)).

FmHA regulations recognize that some borrowers need more assistance than others and that it may be necessary to provide that assistance in a variety of

places. For example, "[s]ome borrower families need supervisory assistance in evaluating and selecting land . . . construction plans and materials, buildings . . . and goods and services at prices they can afford. . . . Such supervisory assistance is especially important with families receiving initial FmHA loans who are relatively inexperienced. . . . With such families it may not be possible to accomplish the objectives of the loan unless effective supervisory assistance is provided at the outset." 7 C.F.R. § 1802.65 (1977).

The regulations instruct the county supervisor to "be prepared with such materials and information as is [sic] needed to effectively assist the family in making the proper evaluation and selection of the goods and services needed." 7 C.F.R. § 1802.65(a)(2) (1977).

Specific regulations, prescribing FmHA policies, methods and responsibilities with respect to planning and performing development work in connection with loans to individuals, require county supervisors to "advise the applicant regarding plans, specifications, cost estimates and other related materials" (7 C.F.R. § 1804.3(f)(2)(iii) (1977)); "[a]dvise the applicant regarding publications, plans, planning aids, engineering data, and other technical advice, and assistance available through local, State, and Federal agencies, and private individuals and organizations" (7 C.F.R. § 1804.3(f)(2)(iv) (1977); "when appropriate, [county supervisors may] offer suggestions as to how plans and specifications might be altered to improve the facility and better serve the needs of the borrower. The county supervisor may assist the borrower in making

revisions to the plans." 7 C.F.R. § 1804.3(f)(2)(vi) (1977).[8]

The regulations further affirm FmHA's responsibility to the borrower in dealings with contractors. All forms and contracts are provided by the agency, 7 C.F.R. § 1804.4(a) (1977), and FmHA may require contractors to provide a surety bond if "[i]n the opinion of the County Supervisor, a surety bond appears advisable in order to protect the borrower against default of the contractor. 7 C.F.R. § 1804.4(d)(2)(i)(b) (1977) (emphasis added).[9]

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[8] All plans for FmHA houses must meet the Minimum Property Standards (7 C.F.R. § 1804.3(d)(1)(i) (1977)), which incorporate "technical requirements for minimum acceptable design, materials and construction methods to protect the interests of the borrower and the FmHA." 7 C.F.R. § 1804.2(d) (1977) (emphasis added).

[9] In fact, when provided, the surety bond must run in favor of the United

Finally, the regulations require the county supervisor to "inspect development work as frequently as necessary to assure that construction and land development conforms [sic] with the plans and specifications," 7 C.F.R. § 1804.4(g)(3) (1977), to record all deficiencies on the FmHA Inspection Report, 7 C.F.R. § 1804.4(g)(4) (1977), and to be "responsible for following up the correction of deficiencies reported on [the Inspection Report]. Id. (Emphasis added.)

The extent of FmHA's control over the borrower and the construction process is graphically illustrated in its standard construction contract. The right to inspect and reject defective materials or workmanship under the contract is

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States as trustee for the borrower. 7 C.F.R. § 1804.4(d)(2)(ii) (1977) (emphasis added).

exclusive to FmHA (J.A. 27).[10] FmHA is the sole arbiter of the amount of work that is in place and consequently the amount that must be disbursed to the contractor when partial payments are made (J.A. 26). The borrower does not even have the right to terminate the contract without the express approval of FmHA (J.A. 27).

Notwithstanding extensive regulations to the contrary, the FmHA argues that its supervision and inspections are primarily for the protection of its security interest and not for the benefit of the borrower (Pet. Br. 23). It reaches its conclusion without

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[10] The regulation requires the borrower to give FmHA prompt written notice of any fault or defect in the work or nonconformance with the contract. 7 C.F.R. § 1804.4(g)(3)(iii) (1977). The regulation does not urge the borrower to notify the contractor of the defect.

significant analysis of the legislative history of Title V or of its own regulations. It draws general analogies between the purposes of the housing acts of 1934 and 1949 while it ignores the very reasons that Title V of the Housing Act of 1949 was adopted, namely that FHA credit and technical services were not available in rural areas. It also ignores that the authority granted FmHA in Section 506 of the 1949 Act has no counterpart in the 1934 Act and that inspections and appraisals conducted by the FHA pursuant to Section 226 of the 1934 Act, 12 U.S.C. § 1715q, were intended to only incidentally benefit the FHA mortgagor. United States v. Neustadt, 366 U.S. at 709.

FmHA attempts to bolster its argument that borrowers are not intended beneficiaries of its inspections by citing a regulation stating that it will not become

a party to the contract between the builder and the borrower nor incur liability thereunder (Pet. Br. 24, n.13). Its assertion with respect to the purpose of that regulation is not supported by any authority. To infer, without support, that the regulation is intended to dispel any reliance by the borrower with respect to FmHA's supervisory and inspection responsibilities reaches far beyond the plain meaning of the regulation.[11]

As further evidence of its position that inspections are purportedly conducted for the sole benefit of the government, FmHA cites to its recent regulations on inspections and states that they clarify preexisting law on the

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11 Although there is a substantial question whether FmHA can avoid making inspections for the benefit of the borrower, if it wanted to dispel borrowers' reliance on its inspections, FmHA could have done so in plain and clear language. See 7 C.F.R. § 1924.9(a) (1982).

issue (Pet. Br. 5, n.1 and 24, n.13). In fact, the regulations reflect the agency's adoption of lower court decisions which concluded, without apparent analysis of the Housing Act of 1949 or FmHA regulations, that § 2680(h) bars a claim against the agency under the Federal Tort Claims Act.

When FmHA published the inspection regulations, the Office of General Counsel (OGC) of the Department of Agriculture had not prepared any memoranda to support the conclusion that inspections were for the sole benefit of protecting the government's security interest. The Director of the OGC Community Development Division has stated that the OGC has no record of written opinions regarding the purpose of inspections but that it had approved regulations that express "established law on this point, i.e., FmHA construction inspections are primarily

to protect the security interests of FmHA and not the borrower. The decision in Ramsey v. FmHA, 443 F. Supp. 760 (E.D. Mo. 1978), sets forth the reasoning and law behind this position." Undated letter from James V. Loughran, Jr., Director, Community Development Division, Office of General Counsel, Department of Agriculture, to Gideon Anders (received May 6, 1980).

Ramsey v. FmHA, supra, does not analyze the legislative history of FmHA's inspection authority. Instead, it adopts the conclusions reached in Adamsville Lumber Co. v. Rainey, 348 F. Supp. 373 (W.D. Tenn. 1972), and United States v. Alice F. Cannon, No. 76-1834 (D.S.C. 1977), neither of which analyzed the legislative history of FmHA's inspection authority. Adamsville and Cannon merely applied to FmHA the decision of this Court in Neustadt and that of other

courts in non-FmHA cases. In short, FmHA's conclusion is not grounded on any provision in the 1949 Act.[12]

Moreover, there is evidence to suggest that the primary motivation for FmHA's adopting the inspection language is the avoidance of liability through litigation. In an April 13, 1978, memorandum to the Director of Program Support Staff of FmHA, OGC wrote:

> This memorandum is a reminder that it is important from a litigating posture that FmHA's regulations be

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12 Even if Neustadt is applicable to FmHA, its holding does not lead to the conclusion that FmHA has no obligations to its borrowers. Neustadt held that the Federal Tort Claims Act does not waive sovereign immunity in misrepresentation cases even if the misrepresentation arises from the performance of a duty specially owed to a program beneficiary. 366 U.S. 707-708. In other words, Neustadt merely held that § 2680(h) precludes a borrower from recovering damages in reliance upon a misrepresentation. It does not purport to determine whether the government owes a duty to the beneficiary. See Bailey v. Romney, 359 F. Supp. 596, 599-600 (D.D.C. 1972).

> revised as soon as possible to indicate that an inspection by FmHA is for security purposes only and not for the borrower's benefit.
>
> Insertion into present regulations of the language found [in] . . . the attached draft would be very beneficial for FmHA, OGC and U.S. Attorneys litigating cases involving improper construction.

Memorandum of Jerome G. Oslick, Attorney, Community Development Division, Office of General Counsel, Department of Agriculture, to George Schladt, Director, FmHA Program Support Staff (April 13, 1979). (Obtained by amicus under the Freedom of Information Act.)

Thus the government's argument that its regulations express long-held statutory interpretations is refuted by its own memorandum.

2. FmHA's liability arises from its negligent supervision and inspection of Ms. Neal's home and not out of a misrepresentation.

It is well recognized that when the government voluntarily undertakes to render services to another and is negligent in the performance of the service, it may be liable for its negligence under the Federal Tort Claims Act. Indian Towing Co. v. United States, 350 U.S. 61 (1955); United Scottish Insurance Co. v. United States, 614 F.2d 188 (9th Cir. 1979); Rogers v. United States, 397 F.2d 12 (4th Cir. 1968); Ingham v. Eastern Air Lines, Inc., 373 F.2d 227 (2d Cir. 1967), cert. denied, 389 U.S. 931 (1967); Wenninger v. United States, 234 F. Supp. 499 (D. Del. 1964), aff'd, 352 F.2d 523 (3d Cir. 1964). Thus, even if the Housing Act of 1949 does not obligate FmHA to inspect

and supervise borrowers' homes, it may be held liable for negligence under Tennessee's good Samaritan rule if it voluntarily undertook to assist Ms. Neal by supervising and inspecting the construction of her home. Park v. United States, 517 F. Supp. 970 (D. Or. 1981), appeal pending, No. 81-3524 (9th Cir., argued Aug. 3, 1982). See Ingham v. Eastern Air Lines, Inc., 373 F.2d at 236; Melton v. United States, 488 F. Supp. 1066 (D.D.C. 1980). See also Rayonier, Inc. v. United States, 352 U.S. 315 (1957); Fair v. United States, 234 F.2d 288, 294 (5th Cir. 1956); United States v. Lawter, 219 F.2d 559 (5th Cir. 1955); Somerset Seafood Co. v. United States, 193 F.2d 631 (4th Cir. 1951).

Ms. Neal alleges in her complaint that she suffered damages as a result of

FmHA's negligent supervision and inspection of her home (J.A. 12). Insofar as her factual allegations must be taken as true, Radowich v. National Football League, 352 U.S. 445, 448 (1957), her complaint should not be dismissed for failure to state a claim unless it appears beyond any doubt that she can prove no set of facts in support of her claim which would entitle her to relief. Conley v. Gibson, 355 U.S. 41, 45-46 (1957).

Notwithstanding Ms. Neal's allegations to the contrary, FmHA maintains that her claim arises out of a misrepresentation (Pet. Br. 14, 16). It argues that the gist of Ms. Neal's claim is that FmHA negligently failed to identify and record certain defects in the construction of her home, and that damages resulted from her purchase of the home

in reliance upon FmHA's representation that the house was without defects (Pet. Br. 17). FmHA thus attempts to bring this case within United States v. Neustadt, supra, which held that the misrepresentation exception to the Federal Tort Claims Act bars a claim against the government for its failure to obtain and communicate information upon which a party may reasonably be expected to rely in the conduct of his or her economic affairs. 366 U.S. 706-707 (1960).

In its zeal, the FmHA overlooks two key elements of the tort of misrepresentation. First, there must be a misrepresentation, i.e., a communication; and, second, the plaintiff must have justifiably relied upon the misrepresentation to her detriment. Ms. Neal relies on neither of these elements to establish her case.

Under Section 226 of the Housing Act of 1934, 12 U.S.C. § 1715q, the FHA had an obligation to deliver its appraisal to Mr. Neustadt; the FmHA has no such requirement either in its statutes or in its regulations. See 7 C.F.R. § 1809.1 et seq. (1977). Ms. Neal has made no allegation that the FmHA delivered an appraisal to her and no evidence is before the Court to suggest that it did. The FmHA also has no statutory or regulatory obligation to provide borrowers with a copy of its inspection reports. See 7 C.F.R. § 1804.4(g) (1977). Although evidence before the Court suggests that Ms. Neal signed such a report, the inspection and signing occurred on October 3, 1977 (J.A. 65), three days after all the funds were disbursed from her escrow account (J.A. 46). Thus, contrary to the government's argument (Pet. Br. 17), Ms. Neal could

not have relied on the inspection report to her detriment. Ms. Neal, therefore, has not and cannot allege that the FmHA has misrepresented the condition of her home.

Ms. Neal has alleged that FmHA undertook to supervise and inspect the construction of her home and to control disbursements to the contractor through the supervised bank account. She further alleged that she relied on FmHA's supervision and inspection to her detriment. Her claim states a simple case of negligence for which the FmHA may be held liable. Park v. United States, 517 F. Supp. 970 (D. Or. 1981), appeal pending, No. 81-3524 (9th Cir., argued Aug. 3, 1982). Parker v. Knebel, No. EC 76-210K (N.D. Miss., Aug. 29, 1978), dismissed on other grounds (N.D. Miss., Jan. 22, 1979). See United States v. White, 429 F. Supp. 1245, 1252, n.7 (N.D. Miss.

1977) (on remand); Melton v. United States, 488 F. Supp. 1066 (D.D.C. 1980). Contra, Reynolds v. United States, 643 F.2d 707 (10th Cir. 1981). See Ortiz v. United States, 661 F.2d 826 (1981), cert. denied, No. 80-2064 (Oct. 5, 1981).

FmHA argues that this case is not controlled by Indian Towing Co. v. United States, 350 U.S. 61 (1955), because "if the FmHA had not been negligent in its inspection of respondent's house, the injury to respondent would still have occurred when the inspector communicated her findings to respondent." (Pet. Br. 11.) The essence of its argument is that the FmHA could not have done anything to protect Ms. Neal from sustaining the damages other than to communicate its inspection results to her. Had FmHA not been negligent in its inspections there are several things FmHA could have done. For example, the county

supervisor should have required the contractor to provide a surety bond. 7 C.F.R. § 1804.4(d)(2)(i)(b) (1977). The county supervisor should also have refused to countersign checks on the supervised bank account, see 7 C.F.R. § 1803.8(d) (1977), rejected the defective materials and workmanship and required the contractor to make repairs (J.A. 27).

FmHA counters that withholding of funds is not supported by statute or regulations, and that it would greatly disrupt the FmHA loan process in a manner that Congress did not intend (Pet. Br. 12). Interestingly, in a 1976 memorandum the OGC suggested precisely that alternative to the FmHA Administrator. It wrote:

> It would appear that FmHA should place more emphasis on proper inspection and corrective action that should be pursued where defects are

> found. For example, the most obvious action where defects are noted is the nondisbursal of remaining loan funds to the contractor until all defects are corrected. [Emphasis added.]

Memorandum of James V. Loughran, Jr., Director, Community Development Division, OGC, USDA, to Frank B. Elliott, FmHA Administrator (Dec. 9, 1976) (obtained by amicus under the Freedom of Information Act).

Congress, in expressing its dissatisfaction with FmHA's inspection and disbursement procedure, has also suggested that the FmHA withhold payments from contractors.

> Most, if not all, of these instances of shoddy construction could have been avoided with proper inspection procedures and appropriate contractual arrangements (such as escrow agreements) with builders. Your committee expects the Secretary to put much greater emphasis on such administrative safeguards so

> that, as a result, the authority provided in [§ 509(c)] will seldom have to be used.

H.R. Rep. 95-236, 95th Cong., 1st Sess. 27-28, reprinted in [1977] U.S. Code Cong. & Ad. News 2884, 2910-2911.

Even assuming that Ms. Neal received the inspection report before funds were disbursed and the inspection report could be construed as a misrepresentation, her claim that the FmHA had an independent duty to carefully inspect and supervise the construction of her home should not fail merely because the FmHA, in addition to negligently undertaking the inspection and supervision, misrepresented the condition of her home. The gravamen of Ms. Neal's claim arises from negligence and not from misrepresentation. Ingham v. Eastern Air Lines, Inc., 373 F.2d 227 (2d Cir. 1967), cert. denied, 389 U.S. 931 (1967); Beech v. United States, 346 F.2d 872 (5th Cir. 1965); United Air

Lines v. Wiener, 335 F.2d 379 (9th Cir. 1964); Melton v. United States, 488 F. Supp. 1066 (D.D.C. 1980); Jordan v. United States, 294 F. Supp. 204 (D. Ga. 1968).

3. The availability of relief under § 509(c) should not be a bar to recovery under the Federal Tort Claims Act.

In Section 509(c) of the 1949 Housing Act, Congress authorized the FmHA to compensate individuals for construction defects which affect the health or safety of the inhabitants. 42 U.S.C. § 1479(c). The Section 509(c) remedy is limited to persons who purchase or contract for the construction of new homes, discover the defects and file a claim within 18 months of the time of purchase or completion of construction. Section 509(c) does not

extend to persons who rehabilitate their homes with loans under either Section 502 or Section 504, 42 U.S.C. § 1474, of the Act, purchase existing homes, or who discover the defect more than 18 months after loan closing or completion of construction. The Section 509(c) program is thus substantially more restrictive than the HUD Section 518 program which is available to purchasers of new and existing housing for a period of 36 months from the time of loan closing. See 12 U.S.C. § 1735b(b).

In adopting the Section 509(c) program, Congress was obviously aware of the problems facing low- and moderate-income purchasers of FmHA housing. Congress perceived the problem as a failure of the FmHA to properly inspect and supervise the construction of housing as it is obligated to do under Section 506 of the Housing Act of 1949. H.R. Rep.

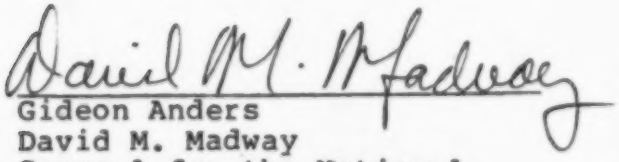
No. 95-236, 95th Cong., 1st Sess. 27-28, reprinted in [1977] U.S. Code Cong. & Ad. News 2884, 2910-2911.

In adopting Section 509(c), Congress did not intend to lessen FmHA's supervisory and inspection responsibility. In fact, it admonished the agency to improve its inspection procedure to eliminate the need for the compensation program. There is no evidence that Congress considered Neustadt in its deliberations or that it intended to make Section 509(c) an exclusive remedy. Id. Absent clear congressional intent to bar Federal Tort Claims Act claims where Section 509(c) relief is available, none should be implied. See United States v. Brown, 348 U.S. 110, 113 (1954); United States v. Muniz, 374 U.S. 150 (1963). See also Kremer v. Chemical Construction Co., 102 S.Ct. 1883, 1890-1896 (1982).

CONCLUSION

The decision of the United States Court of Appeals should be upheld and Ms. Neal should be allowed to proceed with her case.

Respectfully submitted,



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Dated: October 4, 1982

CERTIFICATE OF SERVICE

I hereby certify that three copies of Brief of Amicus Curiae were served upon each of the following individuals by placing these documents in the United States mail, postage prepaid, to:

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Dated: October 4, 1982

David M. Madway

Docket Sheet

NO. 81-1494-CFX	TITLE John R. BLOCK, Secretary of Agriculture, et al., Petitioners v. Onilea NEAL

DOCKETED	COURT
February 9, 1982	U.S. Court of Appeals for the Sixth Circuit

DATE	PROCEEDINGS AND ORDERS
	Counsel for Petitioners: Solicitor General
	Counsel for Respondent:
Feb. 9, 1982	Petition for writ of certiorari filed. (Record filed).
March 3, 1982	Order extending time to file a response to the petition until Apr. 14, 1982.
Apr. 14, 1982	Motion of respondent for leave to proceed in forma pauperis and brief in opposition filed.
Apr. 21, 1982	DISTRIBUTED. 5-13.
May 7, 1982	Reply brief for the petitioners filed. (D).
May 17, 1982	REDISTRIBUTED. 5-20.
May 24, 1982	The motion of respondent for leave to proceed in forma pauperis is GRANTED. Petition GRANTED.

July 7, 1982	Order extending time to file the joint appendix and petitioners' brief on the merits until Aug. 7, 1982.
Aug. 6, 1982	Joint appendix filed.
Aug. 6, 1982	Brief for the petitioners filed.
Aug. 23, 1982	Order extending time to file the respondent's brief on the merits until October 4, 1982.
Oct. 5, 1982	Brief for the respondent filed.
Oct. 6, 1982	Brief, amicus curiae, of Oregon Legal Services Corp. in support of respondent filed.
Oct. 7, 1982	Brief, amicus curiae, of National Housing Law Project in support of respondent filed.
Nov. 17, 1982	CIRCULATED.
Jan. 4, 1983	Reply brief of the petitioner, John R. Block, etc., et al. filed.
Jan. 19, 1983	ARGUED.